POLICY DEBATES

UNDERSTANDING the FREE TRADE Agreement

Edited by
DONALD M. McRAE
and
DEBRA P. STEGER

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Understanding the Free Trade Agreement

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Donald M. McRae
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Debra P. Steger

Proceedings of a Conference held at the University of Ottawa, Faculty of Law (Common Law), January 22, 1988

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Foreword

One measure of the intensity of public debate about the Canada-U.S. Free Trade Agreement signed by Prime Minister Mulroney and President Reagan on January 2nd 1988, is the extent to which legal aspects have become a matter of popular concern. Arcane details of the proposed and existing international procedures for resolution of disputes and the specific nuances of commitments to national treatment are debated over kitchen tables and in the editorial pages.

As a contribution to Canadian discussion of the proposed Free Trade Agreement, the Institute has published a series of studies and conference proceedings which document the stages in the process and are intended to illuminate the key issues. In this activity, the Institute has worked partly from its own research program alone, publishing conference volumes such as *Assessing the Canada-U.S. Free Trade Agreement*, edited by Murray Smith and Frank Stone, which evokes the intensity of the Canadian debate immediately after the dramatic conclusion of the free trade negotiations on October 3rd, 1987. In addition, however, the Institute has collaborated extensively with other organizations, including the Brookings Institution and the Institute for International Economics in Washington, D.C. as well as several Canadian universities, to produce commentaries on this topic. The most recent publications include *The Canada-United States Free Trade Agreement: The Global Impact* (published jointly with the

Institute for International Economics) and *Canadian-American Free Trade: The Sequel* (published with the Center for North American Studies at McGill University.).

The present volume, *Understanding the Free Trade Agreement*, presents the proceedings of a conference co-sponsored by the Institute and held at the University of Ottawa Law School on January 22, 1988. The papers and commentaries presented at the conference provide extensive legal analysis of key issues associated with understanding the policy implications of the Free Trade Agreement. Topics discussed include dispute resolution procedures and the effects of the review mechanism that applies to the trade laws of both countries. Technical aspects of a free trade area and some of the specific issues involved in the elaboration of national treatment are examined. Canadian constitutional dimensions and the issues involved in implementation of the Free Trade Agreement are also considered. Finally, the broader implications for Canada's sovereignty are debated.

Together, these papers provide a thorough analysis by a distinguished group of legal experts and trade policy specialists of the policy implications of the proposed implementation of the Canada-U.S. Free Trade Agreement in the context of Canada's existing international obligations. The Institute for Research on Public Policy is pleased to publish these proceedings of the January 1988 conference in Ottawa as a further contribution to Canadian understanding of the significance of that Agreement.

Rod Dobell
President
September 1988

Avant-propos

Le degré de l'intensité du débat public suscité par la signature de l'Accord de libre-échange Canada/E.-U. par le Premier Ministre Mulroney et le Président Reagan, le 2 janvier 1988, peut se mesurer à l'intérêt que le public a manifesté à l'égard des aspects juridiques de cette question. Les détails les plus subtils concernant les mécanismes internationaux de règlement des différends et les nuances précises des engagements à l'égard du traitement national ont fait l'objet de discussions passionnées autour des tables de cuisine et dans les colonnes des éditoriaux.

L'Institut a contribué au débat général en publiant une série de monographies et les résultats de divers congrès. Ces publications fournissent une documentation sur les étapes successives du processus et permettent d'éclairer les problèmes fondamentaux que cet accord soulève. Pour ce faire, l'Institut s'est servi des travaux effectués dans le cadre de son propre programme de recherches, ce qui a donné lieu à la parution de comptes rendus de travaux de plusieurs congrès, comme par exemple le volume intitulé: *Assessing the Canada–U.S. Free Trade Agreement*, édité par Murray Smith et Frank Stone. Ce volume est un fidèle reflet de l'intensité du débat au Canada, juste après la conclusion spectaculaire des négociations sur le libre-échange, le 3 octobre 1987. L'Institut a également collaboré d'une manière suivie avec d'autres organismes tels quel l'Institution Brookings et l'Institut d'économie internationale de Washington, D.C., ainsi qu'avec plusieurs universités canadiennes. Parmi les plus récentes publications, on en relève une intitulée *The Canada-United States Free Trade Agreement: The Global Impact*; (publiée conjointement avec l'Institut d'économie internationale), et une autre, *Canadian-American Free Trade: The Sequel* (publiée en colaboration avec le Centre d'études nord-américaines de l'Université McGill).

Le présent volume, *Understanding the Free Trade Agreement* (Pour comprendre l'Accord de libre-échange), est un compte rendu des travaux d'un colloque parrainé en partie par l'Institut qui s'est tenu à l'École de droit de l'Université d'Ottawa le 22 janvier 1988. Les communications présentées à ce colloque et les commentaires qu'elles ont suscités constituent une analyse juridique assez complète des questions se rapportant aux répercussions de l'Accord de libre-échange sur le plan politique. Y ont été notamment examinés: les procédures de résolution des différends et les effets des mécanismes de révision sur la législation commerciale en existence dans les deux pays; les problèmes techniques propres à une zone de libre-échange; les questions particulières soulevées par la mise au point du traitement national; les conséquences sur le plan constitutionnel de la mise en application de l'accord; et enfin les conséquences que cet accord pourrait avoir sur la souveraineté nationale canadienne.

L'ensemble de ces études préparées par un groupe de juristes et d'éminents spécialistes en politique commerciale constitue un examen approfondi des conséquences que pourrait avoir, sur le plan politique, la mise en vigueur de l'Accord de libre-échange, dans le contexte des obligations internationales actuelles du Canada. L'Institut de recherches politiques est heureux d'être en mesure de publier les travaux du colloque d'Ottawa de janvier 1988. Il espère ainsi contribuer à améliorer la compréhension que les Canadiens peuvent avoir de cet accord.

Rod Dobell
Président
Septembre 1988

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The Conference was sponsored by the Common Law Section of the University of Ottawa, Faculty of Law, in cooperation with the Institute for Research on Public Policy and the Canadian Council on International Law. Financial support was also provided by the Department of Justice and the Department of External Affairs of the Government of Canada.

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D.M. McRae
D.P. Steger

I.

Introduction

Editors' Introduction

The Canada-U.S. Free Trade Agreement has become the subject of intense public debate in Canada. The details of the Agreement, and their implications for future public policy directions in Canada, have been carefully scrutinized in Parliament, in the press and in popular discussion. Never before has any international agreement, or indeed any policy decision taken by the Government of Canada, received such intense public attention.

The papers in this volume were prepared for the first conference held in Canada to review and assess the detailed text of the Agreement. On January 22, 1988, the University of Ottawa Faculty of Law (Common Law), in coordination with the Institute for Research on Public Policy and the Canadian Council on International Law, sponsored a one-day conference which drew an audience of over 250 people from the Canadian business, government, legal and academic communities.

In this collection of papers, the authors, all leading Canadian and U.S. international trade legal experts or senior officials from the Canadian Embassy in Washington and the Trade Negotiations Office, present a comprehensive and unbiased analysis of the details of this historic Agreement. The Canada-U.S. Free Trade Agreement is an extremely lengthy and complex international agreement. Its 250 page text plus over 1000 pages of Annexes do not encourage ready and accurate comprehension. Despite this, the Canadian public expects, and deserves, a clear and precise understanding of the meaning of specific parts of the Agreement as well as their implications for the future.

Understanding the Free Trade Agreement involves more than a legal interpretation of the text itself. It is also necessary to explain the basic principles of the Agreement in the context of Canada's existing international obligations, including the General Agreement on Tariffs and Trade (GATT) and the related international codes which were negotiated during the Tokyo Round of multilateral trade negotiations. Specific obligations in the Agreement also must be examined in relation to other relevant bilateral and multilateral agreements, such as the International Monetary Fund, the International Energy Agreement, and the various Organization for Economic Cooperation and Development (OECD) Codes.

This book begins with an overview of the Free Trade Agreement. Ambassador Gordon Ritchie, one of the architects of the Agreement, reviews the key elements of the Agreement and explains their genesis in the negotiating process.

One of the critical aspects of the Free Trade Agreement is its dispute settlement mechanisms. In addition to a special binational panel review process for antidumping and countervailing duty disputes, the Agreement contains procedures for government-to-government consultations, modification of new trade measures, further negotiations in some areas, as well as arbitration or resolution of disputes. Under the Agreement, Canada and the United States retain the right to use the dispute settlement procedures of the GATT or the Tokyo Round codes.

Canada and the United States retain the right to use the dispute settlement procedures of the GATT or the Tokyo Round codes for disputes arising under those agreements.

Once a country decides to use either the dispute settlement mechanisms of the Free Trade Agreement or the GATT, it cannot revert to the other process if it becomes disenchanted with the results of a proceeding.

In his paper, Leonard Legault, Minister (Economic), Canadian Embassy, Washington, examines the general dispute settlement mechanisms of the Agreement. Professor Robert Hudec and Julius Katz, both experienced GATT observers, then compare the proposed Canada-U.S. mechanisms with those of the GATT. Debra Steger extends the analysis by comparing the Canada-U.S. provisions with those of other free trade agreements, including the Australia-New Zealand, U.S.-Israel and the European Free Trade Association (EFTA).

The proposed binational panel review system for antidumping and countervailing duty disputes has been subject to considerable debate in Canada. Evaluating this critical chapter of the Agreement requires a detailed understanding of the complicated administrative procedures and substantive provisions of Canadian and U.S. trade laws as well as an analysis of how the proposed review procedures may affect future trade disputes. These issues are examined by leading Canadian and U.S. trade lawyers, Shirley Coffield, Richard Dearden, Gary Horlick, Debra Steger and Debra Valentine.

The Canada-U.S. Free Trade Agreement is a classic free trade area agreement, well within the legal requirements of Article XXIV of the GATT. The Agreement eliminates tariffs and most other restrictive or discriminatory border measures affecting substantially all Canada-U.S. trade within a transition period of ten years from the date the Agreement comes into force. A complex set of rules of origin in the Agreement establish with precision what goods will qualify for preferential or duty-free treatment between the two countries. Details of the phasing in of tariff reductions and the application of the rules of origin are discussed by U.S. tariff negotiator, William Barreda and Alec Macpherson.

Implications of the proposed application of the GATT principle of national treatment in new areas, such as financial services, investment and energy are examined by Carl Lohmann and William Murden, Christopher Thomas and Rowland Harrison. In these new areas, the proposed obligations in the Agreement are compared with those under other existing international arrangements. The authors also give detailed consideration in these papers to the implications for public policy decisions.

Another widely-debated subject in Canada is the question of which level of government, federal or provincial, has the constitutional authority to implement specific aspects of the Agreement. These questions are examined, and debated, in papers by Canadian constitutional authorities, Scott Fairley, William Lederman and Patrick Monahan.

This volume concludes with a debate abcut the implications of the Free Trade Agreement for Canadian sovereignty. Richard Lipsey views the Agreement as a careful and consistent extension of Canada's obligations under the GATT and other international agreements. Liberal Member of Parliament and trade critic, Lloyd Axworthy, argues that the Agreement places significant constraints on the public policy choices of future Canadian governments, while Minister of Youth and Sport, Jean Charest, contends that the Agreement reinforces Canada's position within the multilateral GATT system.

This unique and timely collection of papers presents a comprehensive, reasoned analysis of the Free Trade Agreement based on a thorough knowledge of other international agreements, including the GATT, to which Canada and the United States are signatories. The authors also give careful consideration to the implications of the bilateral obligations contained in the Agreement for future public policymaking in Canada.

The public debate surrounding the Free Trade Agreement has become obscured by emotional rhetoric and misinformation about the details of the Agreement. It is hoped that this collection will contribute to an informed and thoughtful debate of this important subject. For this reason, these papers deserve to be read and reread by anyone seriously interested in understanding this complex, historic Agreement.

Donald M. McRae
Debra P. Steger

II.

Overview of the Free Trade Agreement

The Canada-U.S. Free Trade Agreement

Gordon Ritchie

Let us begin with the Agreement itself: What have we got? Well, we have something that is pretty close to a classical free trade arrangement. I would like to divide my discussion into: the economic (traditional) elements, the sectoral elements, some of the new (pioneering) elements and finally, the institutional elements. These make up the package.

Traditional Elements

Let me begin with the economic elements. The big one, of course, is tariffs. From the outset, we set ourselves the objective of eliminating tariffs entirely. Therefore, the only question to remain was the pace with which they would be eliminated.

After 40 years of trade liberalization bilaterally and multilaterally, we have already eliminated most tariffs on most products crossing the border. About three quarters of the trade both ways is now duty free. The remaining tariffs, by and large, are not dramatic. They average around 5 per cent going into the United States and about 10 per cent coming into Canada. There are, of course, some very important "spikes" among these tariffs. The Agreement will eliminate entirely these remaining tariffs over 10 years. Some will go right away; some will go in 5 years, some in 10. By the end of the transition, all tariffs between Canada and the United States will be gone.

This means that we will have a preferential North American market. We will be prepared, indeed eager, to negotiate the reduction in our external tariffs as part of the multilateral trade negotiations. But until this ultimately comes into place, firms located in Canada are looking for the opportunity to sell into the U.S. market, free of tariffs, against third-country competition which will be facing the MFN tariff rates.

Of course, when you go to a free trade area rather than a customs union, you do not have the bother of going to common external tariffs; but you do have rules of origin, which become critical in order to determine what products qualify for duty-free treatment. The Agreement lays out a complex set of rules of origin which, in our judgment, make business decisions much more predictable. It is a much more transparent system, a much more readable system, and a much clearer and more precise system for determining when a good qualifies. It is based on the new Harmonized System of tariffs nomenclature – a much more elaborate and detailed system than the old one; (the text in either English or French of the American and Canadian schedules runs to some 1 100 pages). By and large, the rules of origin provide that where there is significant change in an imported product, it will qualify. This test will be met when there is a specified change in tariff heading or, in some cases, where at least 50 per cent of the value of the product is the direct cost of processing incurred in Canada or the United States.

Some concern has been expressed regarding the possibility of transshipment into Canada through the United States by way of Mexico. I can assure you that our firm understanding is that we have not only rules, but the enforcement of rules, which will protect against such transshipment. In addition, we will be removing duty remissions, duty drawbacks and duty waivers based upon exports to the United States. This is particularly critical in the automotive sector.

Another element is quantitative restrictions – export or import quotas. In this area, we have built up the GATT rules governing export and import restrictions. These are elaborated further in agriculture and energy. The basic rules are, however, precisely the same for all commodities.

Similarly, in government procurement, we have built upon the GATT system. In the last round of negotiations, we agreed upon a procurement code which identified a number of entities in each country. Contracts let by those entities down to a certain value were open to all countries. That value is about US$171 000. This arrangement will lower that threshold to US$25 000 between Canada and the United States.

Thus in that band (between US$25 000-$171 000), Americans will be able to come into Canada and compete on equal footing with Canadians for government business, and *vice versa*. There is one caveat: this relates only to entities covered by the code. In Canada, this means that it does not cover provincial governments, provincial Crown corporations, any federal Crown corporations, federal agencies, and most of the big federal departments. My guess is that while we were aiming at a $750 billion deal, we may have succeeded in opening up perhaps $250 million of Canadian purchases and perhaps $1 500 million of American.

These are the traditional elements in a classical free tree area. In addition, we have gone a little further in a couple of sectors.

Sectoral Elements

The first of these sectors is agriculture. This, by any historical standard, is a pretty big deal in agriculture. We are eliminating all the tariffs between us.

We have gone to free trade in red meats—in beef and in veal—and these are big-ticket items for our producers. We will be honouring the GATT rules on import restrictions, which means that we have maintained intact our supply management regimes and our capacity to introduce new supply management regimes. Existing regimes cover the dairy and the so-called "feathers" industries: eggs, chicken, turkeys. This was a critical political decision, and it means that consumers, including industrial consumers, will be paying substantially higher prices for the supply managed commodities than if we had been able to go to a free trade arrangement. This also imposes a competitive handicap on the processors. We have been in very close consultation with our processors to work our way around this, and we believe that the impact can be managed, albeit with considerable difficulty.

For fruits and vegetables, we have put in place a contingency protective measure. If we face seriously depressed prices any time over the next 20 years, we will be able to reinstate, for a brief period of the season, the MFN tariff. This affords some protection. The horticultural industry will, nonetheless, face difficult adjustments.

In the related area of alcoholic beverages, we have agreed not to discriminate against American wines. This will be phased in over seven years. From the Americans' point of view, we are simply phasing in the agreements already made in the Tokyo Round of negotiations, based upon the firm commitments of the Ontario premier and the Canadian government which the Americans believe we have failed to live up to. This view is shared by the Europeans, and there is a major GATT case in progress at the present time. While the bilateral arrangement proceeds independently, it does so against this background. The Agreement will, over seven years, provide the Americans with something similar to so-called "national treatment" for listings in markups and distribution.

Beer is not covered by the Agreement, although it forms a major part of the GATT negotiations. Spirits are covered, in the sense that we have preserved our free access to the U.S. market, and have gained some improvements to that access.

The second major chapter is related to energy. We have, basically, enshrined our present energy policies. This chapter of the Agreement has come under intense attack on Capitol Hill as a major sellout by the U.S. administration. The American oil and gas producers are furious because it means that the United States will not be able to apply import restrictions, charges, surcharges or duties on imports of Canadian oil and gas. The uranium producers have been vociferous in their opposition to the removal of the embargo, which has threatened our market for uranium in the United States, worth about $300 million a clip. The coal and electricity producers are furious because the coalition they were building (with some success) to block exports of hydro power (notably from Manitoba) to the United States, faces a major setback with this Agreement. This means that we have secured our access to the United States market. We have done so on a basis which we believe will permit a more economical development of Canadian energy resources.

We have, of course, retained the capacity to restrict our exports in the event of short supply. We will do so on a basis which will ensure that our customers in good times remain customers, treated fairly, in tough times; we have established certain "proportionality" formulas to govern this.

If we are obliged to apply restrictions to our exports, there may be some significant divergence of price between the United States and Canada, since the American price outstrips ours. But both countries have agreed not to explicitly or directly intervene at the border to discriminate on price.

That, in a nutshell, is the government's energy policy enshrined in a bilateral agreement which preserves our access to the United States. As I say, it is a very controversial item in the United States. It has, somewhat to my surprise, caused some initial controversy here, although this seems to have eased considerably as people have come to understand what is actually in the Agreement.

The same comment could apply to the automotive sector. In our judgment, and in the judgment of industry analysts, the Agreement offers fairly significant benefits in terms of North American output and employment, and we expect to get our share of those benefits. The autopact safeguards are fully intact. In order to qualify for autopact treatment, a company will have to meet the assembly ratio requirement and the CVA commitments. This applies to all the existing qualified manufacturers as well as any who are able to qualify between now and the end of the 1989 model year – which in practice means the Big Three plus Suzuki in its joint venture with General Motors. These companies, provided they qualify and they remain qualified, will be able to import duty free from anywhere in the world. If they fail to meet the safeguards, they will lose the privilege, which is currently worth about $300 million per year to them.

For the rest of the trade, cross-border tariffs will be phased out like other tariffs over the next 10 years. Some will disappear faster; aftermarket parts will be phased out in 5 years. As for other products, there will be a rule of origin which will provide that 50 per cent of the value of the product must have been involved in the direct cost of processing in Canada or the United States.

We will also be phasing out duty remission programs. The only ones that are significant are those which we have extended to the recent transplants: Honda, Toyota, Hyundai. We will fully honour the commitments we have in our contractual arrangements with them. The duty remissions programs will expire as the commitments expire, no later than 1996.

That is the automotive package. The autopact remains in place and, in addition, there will be free trade between the two countries for goods meeting the rules of origin. As a footnote, we are eliminating embargo on used cars (which outlived its usefulness some years ago).

Pioneering Elements

Let me turn to the pioneering elements of the Agreement: services and investment. This is new territory for Canada, and indeed any other country, in international trade agreements.

The service industries will probably be major beneficiaries of this Agreement, not because of the specific provisions of the Agreement – which are in fact quite modest; they cover a relatively small proportion of service employment – but because they will benefit most from the general increase in disposable incomes in the United States and, in particular, in Canada. The Agreement provides principles for future regulations, essentially that we will not discriminate in future regulation. We are free to regulate, but not on a basis that artifically distinguishes between Americans and Canadians on either side.

In addition, there are some modest sectoral agreements in the profession of architecture, tourism, enhanced telecommunications and computer services as well as one not-so-modest services agreement on financial services. The latter agreement provides us with security of treatment in the United States – which in some cases, incidentally, is better treatment than that given American financial institutions. On our side, we will be removing some discriminations against American ownership. They will be subject to the same rules as Canadian owners and institutions. I have to admit that although this is an important agreement it pales in its impact in comparison to the revolution that is going on in the world of financial industries generally, as reflected in the federal financial legislative reform and the Ontario financial legislative reform, which will themselves bring about major changes in the operation of the industry. This agreement, in a sense, recognizes these changes and will provide a bit of underpinning for them in the future.

In addition, under the broad heading of services we have made some interesting progress in freeing access of temporary personnel to one another's countries. We are not talking about blue collar workers and we are not talking about immigration. We are talking about a limited number of categories, where the Canadian business community told us loud and clear the they faced increasing problems at the border in providing personnel to deliver services, aftermarket services and after sales services.

Essentially, the arrangement will provide that Canadians are given special status crossing the border. Special arrangements will be put into place in order that Canadian citizens can provide the kind of service in the United States without having to put on sneakers and a Hawaiian shirt every time they come to the border.

In addition, the cultural industries, broadly defined, have been excluded from the Agreement. The Agreement is unequivocal on this. The definition of cultural industries is very broad indeed. As a footnote, this means that the cultural industries are excluded from the benefits and disciplines of the Agreement.

Essentially, the investment chapter enshrines present investment policies. This means that all of the existing restrictions remain in place – energy, transportation, communications, culture, etc. Outside these specific sectoral policies, new investments will be free, as they are now. When takeovers are involved, we have agreed that over three years we will move to a regime where we will no longer be reviewing American indirect takeovers to Canadian enterprises, and we will be reviewing only those direct takeovers of assets in excess of CAN$150 million.

I have to admit, however, that the main impact on investment will not be found in this chapter. The main impact will be the judgment of investors, Canadian and foreign, whether the Agreement does, in fact, provide them with substantially enhanced access to the North American market as a whole, and whether that access is indeed secure.

Institutional Elements

Security of access is a big issue for Canadians, and has formed the basis of what I have labelled the "institutional package." Let me take a moment to speak on this.

First, there is a Canadian-U.S. Trade Commission which is essentially a political apparatus for the overall management of the Agreement. But there will be disagreements. There will be disputes and they will have to be resolved. To resolve them there is a general system which will involve GATT-type panels. There will be rosters of Canadians and Americans. A panel will be formed of two Canadians, two Americans and a fifth person chosen from the roster who is acceptable to the other four. If the four cannot agree, the two governments will work it out. If the governments fail to reach an agreement, the fifth person will be chosen by lot (it is worth noting that both countries are going to name at least one unacceptable candidate to the roster such that the other side will be very reluctant to risk going by lot, and will instead encourage agreement at an earlier stage). These panels will be comprised of trade experts. The majority will be lawyers.

This process shares the strength of the GATT panel resolution device, but it also shares its weakness. The weakness is that at the end of the day the panel makes a recommendation that you can accept or reject. The parties are bound only if they agreed in advance to be bound, which of course they would never do if they had a weak case. This sort of binding provision is never used, as they were never used in the International Joint Commission (IJC).

This package, incidentally, was the farthest that the Americans were prepared to go under this Agreement, until the end of September. It was unthinkable that they would go farther than that.

We had to have more. The first thing Canada had to address was import safeguards, which occur when either country feels that its industry is getting injured by a flood of imports from the other country. The countries are not claiming that this is unfair trade, nor are they claiming that this is subsidized or dumped; they just don't like the heat.

The provisions in the Agreement represent a substantial improvement over the international rules that now apply. Basically, what they say is this: while we are lowering tariffs, if the lowering of tariffs in itself causes an import flood, then we will have the right to go back to the old MFN tariff, for a brief transitional period. Once the transition is over, no more safeguard actions will be possible.

The tougher case is where one country, for example the United States, applies restrictions against the world. What does this do to Canada? The answer is: it does not include Canada unless Canada is a significant part of the problem (particularly if there are transshipment difficulties, although we think we will be able to deal with those through our rules of origin procedures). If Canada is a big part of the problem, then the United States can put a restriction on us. The restriction will have to be at a high level which allows for Canada's historic level of trade plus growth of that trade, and the United States will have to provide us with compensation. If we don't like what they have done, then we can take them to a panel. But this time the panel decision is binding in advance, automatically. The panel will rule on whether the United States was right to impose a restriction on us, whether the restriction was at the right level and whether Canada received enough compensation.

The toughest area of U.S. trade law, however, is in relation to countervail and antidumping. Canada strived for clear and predictable rules, objectively applied. The Americans could not swallow that. We could not agree on a new set of rules because the rules we were insisting they accept were too tough for them to swallow. Really, it was that simple. So we failed. We did, however, reach a compromise.

Canada sought a high level of discipline on U.S. trade remedies in exchange for a high level of discipline in Canadian subsidies. In the end, there was no additional discipline on subsidies, and a reduced but significant level of discipline on trade remedies.

The compromise has three elements. First, Canada has not given up on a new set of rules. We will be working on this over the next five years and we will give ourselves another two if we need it. That is going to be tough negotiation. I think we will probably achieve our objectives on antidumping fairly quickly because we were close to agreement in this area. But the issue of subsidies is going to be very, very tough.

In the interim, if the American legislative base changes it will not apply to Canada unless we are specifically named. Almost never in their legislative history have the Americans specifically named a country in any of their trade legislation. They would have to name Canada for the legislation to apply to us, and if they did, and we did not like the legislation, the issue would go to a panel and the panel would make a binding declaratory finding. The panel would determine whether the Americans had fully respected our GATT rights, our rights under the Agreement, and any prior decisions of the panel.

While this is all well and good, meanwhile there are cases that are going to have to be reviewed by the panel. The panel is a revolutionary mechanism; for the first time in U.S. history, U.S. law and its interpretation by U.S. authorities will be subject to review by an international, impartial panel. The panel will determine whether the decision was right in law, whether it was supported by the facts and whether it was consistent with prior panel decisions. Furthermore, this will be completed in a short time frame. This, in our judgment, is a significant improvement over the security we now enjoy. It does not go as far as we would have liked in terms of an entirely new set of rules. On the other hand, it preserves our domestic freedom of action.

Next Steps

The Agreement was signed on January 2, 1988. We are now in the implementation stage. This is going to be an exhaustive, not to say an exhausting process. Canadian legislation with appropriate bills will be tabled by April/May 1988. It will be studied by the House and Senate. There will be extended committee hearings to scrutinize that legislation.

Meanwhile, the Americans have their own way of doing things. Their legislators have suggested that the bill to approve the Agreement and to put it into law will be tabled the beginning of June 1988. At that point, Congress will have to vote "yes" or "no" on the Agreement with no scope for amendment.

The administration is pressing for an earlier time track for this legislation. There is also a wildcard – the omnibus or "ominous" trade bill, which is running around the same time through the same body – which we can discuss in question period. But the bottom line is this: although we have signed an agreement between heads of government, it will be ratified and will enter into force only if it is enacted into law by the legislatures in both countries, on the basis of legislation which is satisfactory to both countries. There will, in addition, be a number of administrative and regulatory changes. We are confident, however, that this will be managed and that we will be up and running for the first of January 1989.

III.

Dispute Resolution

Institutions and Dispute Settlement Procedures under the Canada-U.S. Free Trade Agreement

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L. H. Legault

The Canada-U.S. Free Trade Agreement (FTA) is a striking achievement as it stands. It brings under the discipline of agreed rules an economic and trade relationship of unique closeness and complexity. It gives the relationship a greater mutuality and defines a common object and purpose for the parties. It provides the parties with the means to ensure implementation of the Agreement and to manage their relationship more effectively, in particular by means of a pioneering system of dispute avoidance and dispute settlement.

What is less obvious but no less important than an immediate achievement is the potential one, for the Agreement is like a living thing in that it embodies a capacity for growth. Indeed, it sets the direction for that growth and establishes the institutions that will nurture the process. In this sense, the FTA represents not so much the end as the beginning of an initiative. Capacity for growth, however, does not mean capacity for metamorphosis, and the Agreement is and will remain no more than a commercial arrangement – albeit one of grand proportions.

The provisions of the Agreement relating to its implementation, further elaboration and the avoidance and settlement of disputes, are of critical importance. If these work, the Agreement works. I shall attempt to give you a brief but comprehensive review of these three functions. They are, of course, closely interrelated and they overlap to some extent, so that the choice of one heading or another is necesssarily arbitrary in some cases. The overlap, for the most part, is obvious. But it should be emphasized at the outset that dispute settlement has a direct bearing on further elaboration of the Agreement.

Central to the fulfillment of all three functions is the Canada-U.S. Trade Commission established by Article 1802. This article charges the commission with the responsibility to supervise the implementation of the Agreement, to oversee its further elaboration, to resolve disputes over its interpretation and application, to review its functioning at least once a year, and to consider any other matter that may affect its operation. The principal representatives of the parties on the commission will be the cabinet-level officer or minister primarily responsible for international trade in each country, or their designees. The commission may establish *ad hoc* or standing committees or working groups, and may seek advice from non-government sources. Decisions of the commission will be by consensus.

Canada and the United States have made it clear that the primary responsibility for the application of the Agreement rests with the two governments themselves. Thus, the Canada-U.S. Trade Commission is in no way an independent body or a kind of "third party" to the agreement. Indeed, it is the parties themselves and not the commission that must be given notice of any measure that might materially affect the operation of the Agreement (Article 1803). Similarly, it is the parties and not the commission who must enter into consultations on any matter alleged to affect the operation of the Agreement (Article 1804). The commission comes into play only if direct consultations between the parties fail to resolve an issue.

While the commission is clearly the central institution under the Agreement, a number of subsidiary bodies are created for specific purposes. With regard to the implementation of the Agreement, there are four subsidiary bodies. These are:

- a working group to review levels of government support for wheat, oats and barley (Annex 705.4)
- a joint monitoring committee to monitor and report on progress in the further elaboration of technical regulations and standards in respect to agricultural products (Article 708 and Annex 708.1)
- a consultative mechanism to review the implementation of provisions relating to the temporary entry of business persons into the territory of each party (Article 1503)
- a permanent Secretariat to facilitate the implementation of provisions relating to binational dispute settlement in antidumping (AD) and countervailing duty (CVD) matters,

with offices in the District of Columbia and the National Capital Region of Canada (Article 1909).

With regard to further elaboration of the Agreement, the expansion and enhancement of benefits through further cooperation is expressly included among the parties' general objectives (Article 102). This is not a simple pious hope. It is backed by detailed commitments scattered throughout some 300-odd pages of text. Thus, negotiations are to be undertaken to harmonize nonagricultural technical standards (Article 608); to expand the provisions on government procurement (Article 1307); and to improve those on trade in services (Article 1405), including the development of mutually acceptable professional standards and criteria for architectural services (Annex 1404-A). Consultations are to be pursued with a view to facilitating the tourist trade (Annex 1404-B), and to further facilitate temporary entry for business purposes (Annex 1503).

In addition, 11 subsidiary institutions are established for further elaboration of the Agreement in various areas. These institutions are:

- a total of eight working groups on technical regulations and standards in the field of agriculture (Article 708)
- a select panel on North American automotive trade and production (Article 1004)
- a working group on rules and disciplines concerning government subsidies and unfair pricing (Article 1907)
- a joint advisory committee on outstanding issues related to retransmission rights (Article 2006(4)).

With regard to the avoidance and settlement of disputes, the provisions of the Agreement are especially elaborate. Professor John Jackson in his classic text points out that "[t]here is no single, sharply defined dispute settlement procedure in GATT that can be readily distinguished from the remainder of GATT activity. Or, in the alternative, one can say that there are over 30 such procedures." A similar observation could be made about dispute settlement procedures under the FTA. Nonetheless, for the sake of convenience, the provisions may be divided into four systems, although other commentators might adopt a different breakdown.

The first system is the general one governing most disputes. This system comprises a range of procedures, including notification and consultation, recommendations by binational panels of experts, binding arbitration by special agreement between the parties (Chapter 18) and compulsory binding arbitration on safeguards or escape clause actions not resolved by consultation (Article 1103 and Article 1806).

The second system comprises binational panel procedures to review and issue declaratory opinions on amendments to a party's AD and CVD laws (Article 1903), and to review and make binding decisions on final orders in AD/CVD cases (Article 1904). The latter panel decisions may be subject to review by an extraordinary challenge committee in exceptional circumstances (Article 1904).

The third system comprises the dispute settlement procedures available under the GATT. These are retained for issues arising under both the FTA and the GATT, the choice of forum being left to the complaining party (Article 1801).

The fourth system comprises a number of sectoral procedures (various articles) and a special provision for joint or separate intervention in domestic judicial or administrative proceedings (Article 1808). The sectoral procedures are as follows:

- consultations on uniform administration of customs measures, and notification and consultation prior to major changes in such measures (Article 406 and Annex 406)
- compulsory binding arbitration on the determination of levels of government support for wheat, oats and barley (Annex 705.4)
- consultations on regulatory matters in the field of energy (Article 905)
- review of compliance with agreed professional standards and criteria for architectural services by a special committee established for this purpose (Annex 1404)
- panel recommendations or binding arbitration by special agreement for disputes regarding the interpretation or application of the Agreement's investment provisions, excluding decisions on proposed acquisitions that are subject to review by Investment Canada (Article 1608)
- consultations on financial services between the Canadian Department of Finance and the U.S. Department of the Treasury, and prior notification of any change in the regulation of such services (Article 1704)
- review of Canadian plywood standards by a special panel of experts if this issue is not otherwise resolved (Exchange of Letters).

By now you may have concluded that government lawyers in Canada and the United States were determined to ensure unlimited forum shopping or lifetime employment for bureaucrats on some working group, panel, committee or whatnot. However, the maze of procedures and institutions described thus far is not so bewildering nor so fragmented as it may appear. Indeed, there are essentially two basic systems only: the general one and the particular one for AD and CVD matters. The retention of GATT procedures for some matters is optional, and the various sectoral procedures embody only a few departures from the general system.

Against this backdrop, it is possible to summarize the steps that would normally be invoked for the avoidance and settlement of disputes under the general system. Each step assumes no resolution of the dispute at the immediately preceding stage. Thus, the procedures unfold as follows:

- a party provides advance notification, whenever possible, of any proposed or actual measure that might materially affect the operation of the Agreement (Article 1803)
- the parties enter into direct consultations upon request (Article 1804)
- the commission institutes its own consultations at the request of either party (Article 1805)
- the commission may call upon technical advice or mediation by a third party (Article 1805(2))
- binding arbitration may be invoked by consensus of the commission or, respecting safeguards, at the instance of either party (Article 1806)
- a dispute not resolved by the commission or not referred to arbitration may be referred to panel procedures at the instance of either party (Article 1807)
- the panel issues its preliminary report with findings of fact, a determination whether the measure at issue is consistent with the Agreement, and recommendations for resolution of the matter (Article 1807(5))
- either party may present objections to the report, which may then be reconsidered by the panel (Article 1807(6))
- the panel issues its final report (Article 1807(7))
- the commission agrees on the resolution of the dispute, normally in conformity with the recommendations of the panel (Article 1807(8))
- failing agreement within the commission and assuming impairment of rights or benefits, the complaining party may retaliate by suspending benefits of equivalent effect (Article 1807(9)).

The time limits for each phase of this general dispute settlement process ensure a resolution within eight to nine months. Panelists will be experts and will normally be chosen from a roster established by the commission (Article 1807(11)). Each panel will be composed of five members, at least two of whom will be citizens of Canada and at least two of whom will be citizens of the United States (Article 1807(2)). Each party will appoint two panelists and the fifth will be selected by the commission, or by the first four panelists, or by lot, as may be necessary (Article 1807(2)). Panels will normally establish their own rules of procedure, subject to certain minimum requirements (Article 1807(4)).

The system for avoidance and settlement of disputes in AD and CVD matters incorporates a number of special features going beyond the general system. These are of particular interest and can be briefly summarized.

First, the Agreement provides that changes to existing U.S. or Canadian AD or CVD laws will not apply to the other country unless the amending legislation so provides in explicit terms and unless there has been prior notification and consultation where requested. Moreover, such changes must not be inconsistent with GATT agreements or with the object and purpose of the FTA. Disputes regarding amendments to AD and CVD laws are subject to compulsory arbitration by a binational panel to determine whether they are consistent with GATT agreements and the object and purpose of the FTA, or (if consistent) whether they have the function and effect of overturning a prior decision of a binational panel. If the panel recommends modifications to the proposed legislative amendments, the parties must consult with a view to reaching agreement on such modifications. Failing agreement, the complaining party may take comparable legislative or equivalent executive action, or may terminate the Agreement (Article 1903).

Secondly, final orders in AD or CVD proceedings will be subject to review by a binational panel at the request of either country (Article 1904(2)), on its own initiative or where called for by a private party who would otherwise be entitled to commence domestic review procedures (Article 1904(5)). Binational review will replace domestic judicial review (Article 1904(1)), but will apply the standard of judicial review applicable under the law of the importing country (Article 1904(3)) to determine whether the AD or CVD order was in accordance with the law of that country (Article 1904(2)).

Panel findings under this procedure are binding (Article 1904(9)). If the panel finds that the law of the importing country was properly applied, the matter is closed. If the panel finds that the body issuing the AD or CVD order was in error, it may remand the order to that body for action not inconsistent with the panel decision (Article 1904(8)).

To ensure the integrity of the process, where either country considers that there has been gross misconduct, bias or serious conflict of interest on the part of a panel member, or that a panel has manifestly exceeded its jurisdiction, an extraordinary challenge committee may be established to review the binational panel's decision (Article 1904(13)). The committee will comprise three members chosen from a roster of judges or former judges from both countries (Annex 1904.13(2)). Decisions by this "court of last resort" must be given within 30 days and will be binding on both countries (Annex 1904.13(3)).

The binational panels for AD and CVD matters will be composed of five members and will normally be chosen from a special roster of Canadian and U.S. nationals to be established by the parties before the Agreement's entry into force (Annex 1901.2(2)). Each party chooses two panelists, subject to peremptory challenges (Annex 1901.2(2)). The fifth panelist is selected by agreement between the parties, by the first four panelists, or by lot, as may be necessary (Annex 1901.2(3)). Because of the judicial nature of the review process, the majority of the panelists must be lawyers (Annex 1901.2(2)). A panel must render its final decision within 315 days (Article 1904(14)).

Rules of procedure for panels reviewing proposed legislative amendments will be established by the panels themselves (Annex 1903.2(1)). Detailed rules of procedure for panels reviewing final orders in AD and CVD cases and for the extraordinary challenge committee, will be established by the parties by the time the Agreement enters into force (Article 1904(14)).

The binational review mechanism for AD and CVD matters will be in place for a period of five years, with provision for a two-year extension (Article 1906). During this period, a joint working group will seek to develop a "substitute system" of agreed rules and disciplines to be applicable in both countries (Article 1907). Failure to reach agreement on such a system would allow either party to terminate the Agreement upon six month's notice (Article 1906).

Having reviewed the dispute settlement procedures to be available under the Agreement, a brief comparison with the procedures available until now may be instructive. Both the general system and the antidumping and countervailing duty system of dispute settlement under the Agreement incorporate significant improvements on GATT procedures. The time limits are certain, whereas they are indeterminate under most GATT agreements. Other countries cannot intervene to complicate and delay matters, as they can in the GATT system. In some matters, proceedings may be instituted at an earlier stage than is possible under GATT. Panels may not be blocked from adopting their reports. Remedies under the

FTA are direct and more effective and, for some important matters, are to be binding upon the parties, whereas GATT panel decisions are not. The independence of the panels is better assured since government officials are barred from participating, whereas GATT panels are almost always chosen from diplomatic missions in Geneva. Finally, by limiting the choice of panelists to Canadian and U.S. nationals (with the possible exception of one panelist under the general mechanism), the FTA will ensure familiarity with the issues and with North American legal traditions.

The FTA's special provisions for AD and CVD matters also incorporate significant improvements to judicial review procedures under the existing laws of Canada and the United States. Here too the time limits will be shorter and more certain. The binational character of the panels will encourage a better balance between Canadian and U.S. views on the applicable law, and above all, a greater perception of fairness and objectivity. The cost of appeals will no longer frustrate the rights of small businesses since they will be entitled to have their views presented by their government before a binational review panel.

Perhaps most important of all, the FTA affords each country a new and unique form of protection from future changes in the other country's AD/CVD laws. Existing procedures provide nothing comparable. The need to debate whether legislative changes are to be made applicable to the other country should help to restrain protectionist elements in both Congress and Parliament. The prospect of binational review of any changes will add another measure of discipline. The final deterrent will be the risk that the Agreement as a whole might be lost as a result of inappropriate changes and refusal to modify them in accordance with a panel's finding.

Finally, the FTA offers a new and significant measure of protection for each party in respect of the other party's laws on safeguards or escape clause actions which place temporary restrictions on imports, causing serious injury to domestic producers. The risk of being "sideswiped" by such actions when they are aimed largely at other countries will be greatly reduced by the establishment of strict thresholds and other conditions (Article 1102). As already noted, disputes in respect of such actions will be subject to compulsory arbitration.

In conclusion, it should be emphasized that the FTA confirms and develops fundamental principles of international law on the settlement of disputes, and it builds upon a long tradition of peaceful resolution of disputes in Canada-U.S. relations. It gives innovative effect to Article 33 of the United Nations (UN) Charter and the Declaration of Principles of International Law Concerning Friendly Relations Among States. Furthermore, it transforms into an effective legal commitment the first principle set out in the report of Ambassador Heeney and Ambassador Merchant to Prime Minister Pearson and President Johnson in 1965. Nearly a quarter of a century ago, the principle enunciated by the two ambassadors called for consultations to"... be initiated whenever one of the two governments is in the process of formulating important policies or planning actions which would have an appreciable impact on the other." Henceforth, virtually all actions with a bearing on that trade relationship will indeed be the subject of notification and consultation, and of dispute settlement procedures if necessary, based on agreed rules and normative standards in furtherance of a common object and purpose, within a structure of institutions that will take the work forward.

The Agreement, in sum, brings the rule of law and a system of law to the trading relations of Canada and the United States. It establishes not only primary rules and principles, but secondary rules of procedure for the further development of the law. There is here a solid foundation for the elaboration of the new regime of North American trade remedy law projected for establishment within a period of five to seven years.

The FTA Provisions on Dispute Settlement: The Lessons of the GATT Experience

Robert E. Hudec

My assignment is to describe the experience of the General Agreement on Tariffs and Trade (GATT) with dispute settlement procedures, and to comment on the possible lessons that experience may have for dispute settlement under the Canada-United States Free Trade Agreement (FTA). Given that I am speaking to an audience composed largely of lawyers and government officials, I believe I can be most helpful by devoting most of my time to presenting information about GATT and its problems, saving a brief time at the end to point out the fairly obvious parallels between the GATT's problems and those likely to arise in dispute settlement under the FTA.

A Brief History of GATT Dispute Settlement

GATT dispute settlement procedures were not provided for in the original General Agreement of 1947, nor were they laid out by any subsequent legal text. GATT dispute settlement procedures have developed over the years through a series of *ad hoc* decisions and experiments, as the GATT felt its way cautiously over unmapped and frequently very hostile terrain.

The original 1947 GATT agreement was supposed to be a provisional trade agreement, designed to last only a few years. The

1947 text contained only one brief provision, Article XXIII, which authorized the Contracting Parties to receive, examine and rule upon legal complaints from a member country. Nothing was said about how the Contracting Parties were to do any of this.

The first lawsuit in GATT history was quite different than the procedure we see today. It occurred in August 1948, during the second meeting (Session) of the Contracting Parties. The delegate from the Netherlands asked the chairman whether a Cuban consular fee of 5 per cent *ad valorem* for goods from the Netherlands and 2 per cent for goods from most other countries were consistent with the MFN obligation of GATT Article I. The chairman of the Contracting Parties during these years was the Honourable L. Dana Wilgress of Canada, one of the GATT's founding fathers and its chairman for the first five years of its existence. Wilgress said, "No." That was it. Cuba did not speak, neither did anyone else, except for an information question on a related issue. The legal ruling was printed in the GATT document series a few years later – the GATT's first authoritative legal decision. Article XXIII was not even mentioned.

The "Chairman's Ruling" was an appropriate dispute settlement procedure for the GATT of this period. In 1948, the GATT was a relatively small organization with only 23 member countries, most of whom were represented by the commercial policy diplomats who had drafted the GATT and the ITO Charter during the preceding two years. This was a group that could recall with considerable confidence not only what they had written and why, but what they would have written if some other question had been raised.

That was forty years ago. The GATT is a much different place today, and so is its dispute settlement procedure. Both GATT and its procedures have evolved to meet the needs and desires of the changing environment.

For the most part, the development of the dispute settlement mechanism has come about through initiatives taken by the GATT Secretariat in response to perceived failings of existing arrangements. Changes have normally been put into effect quietly, sometimes surreptitiously. When changes gained acceptance, they would usually be recognized in some document or other – 3 or 5 or 10 years later. The few changes attempted by legislating new rules or procedures – most conspicuously, the time limits and conciliation procedures of certain 1979 Tokyo Round Codes – have tended to fail.

The process of *ad hoc* experiment continues today. The current Uruguay Round negotiations are scheduled to consider a comprehensive reform of the existing dispute settlement machinery, but it is unlikely that change will occur as the result of any single, comprehensive act of reform. Rather, what will probably happen is that good ideas submitted for consideration will be put into practice by the Secretariat right away; so will any new ideas developed by the Secretariat itself. The final protocol will probably announce with great fanfare the creation of something that is already in place.

The GATT Dispute Settlement Procedure Today

The following is a rough outline of GATT's current procedures:

A government with a legal complaint must first conduct bilateral consultations with the other party. This can be done without any formal notice to GATT, although it is frequently made public to gain attention.

If bilateral consultations fail to produce a solution, the complaining party will then ask the GATT Council to create a panel to rule on the legal claim at issue. Since the GATT Council acts only by consensus, the defendant has the power to block the creation of a panel; but the right to a panel is by now so well recognized that, in practice, the blocking power can be used only to delay the process for a meeting or two, and then only if the defendant has a decent excuse, (such as inadequate time to prepare or inadequacy of the consultation procedure). When the Council decides formally that a panel should be appointed, it delegates to the chairman of the Council the job of appointing the individual panelists and defining the panel's terms of reference.

In fact, both panelists and terms of reference are established by agreement between the parties, and the chairman himself is seldom involved in the process. The GATT Secretariat performs the search for qualified panelists, and drafts proposed terms of reference; it then brokers the disputing parties' agreement to both panelists and terms of reference. Only when this has been done does the chairman of the Council announce the result as his decision.

The normal number of members on a GATT panel is three. Panels of five members have been used on occasion, although at present they are generally thought to be too large – an impediment to quick and sharp decisions. The chairman of the panel is, if possible, one who holds or has held ambassadorial or chief-of-delegation rank. In the past, almost all panel members have been selected from GATT delegations of "neutral" countries, under an assurance that they will be "acting in their personal capacity" – that is, not under instruction from their government. Today, an increasing number of non-governmental persons are being selected as panel members: chiefly retired GATT diplomats, retired Secretariat officials and professors.

In the past, terms of reference were often a source of delay as parties jockeyed for advantage. Today, such battles tend to be rare (they were almost never won); the parties normally accept standard terms of reference which say little more than, "Write a report and make a legal finding on the complaint." Recently, however, terms of reference have become a source of delay because of pressures from third countries, particularly developing countries who want to make certain that the panel report will not threaten their own practices or other interests. Under the principle of consensus decision making, third countries can, if they so desire, block things until their own concerns are met.

When the panel is finally in place, the first step is an organizational meeting with the parties in which procedures, by now fairly standard, are agreed upon. Often only the panel chairperson shows up. As a practical matter, this meeting could well be conducted by mail.

The first substantive event in the panel's proceedings is the submission of party statements. The statements tend to be somewhere between briefs and diplomatic statements, depending on the author. Unlike briefs submitted to domestic courts, GATT practice is that party statements are submitted simultaneously, a practice which may soon be changed because it makes party presentations significantly less helpful than they might be. The parties have about three to four weeks to submit their briefs.

Then comes the first meeting, a week or two after the submission of first statements. (All time periods become stretched a bit when out-of-town panelists are involved because of the extra time needed to transmit papers. Time periods are also extended, of course, by certain blank spots in the calendar – a long Christmas break, the month of August, important GATT meetings). At the first meeting, the parties state their positions, respond to each other, and either answer or take note of questions from the panel. The character of advocacy at these meetings varies by country: the United States almost always has a lawyer; the European Community has generally preferred representation by diplomats, but has been represented by lawyers more and more frequently; other delegations tend to rely on local diplomats who may or may not have legal training.

Next comes a second round of briefs and meetings – called rebuttal. The utility of this round depends on how well the issues have been defined at the first meeting – the quality of the first arguments, and the quality of the panel's response to them. The second round takes another month to six weeks for briefs and argument.

The panel then meets *in camera* following the second meeting and usually comes to a tentative decision at this point. This is when the process of writing a report begins. Step One is the preparation of a first section containing a summary of relevant facts and arguments. The Secretariat will usually draft this part of the report and, after the panel reviews and revises it, the draft will be sent to the parties for comment. Step Two is the preparation of a second section containing a decision on the merits. Once the panel has reached a tentative decision on the merits, it will start the drafting process by instructing the Secretariat (or a panel member) to draft a fuller statement of the legal conclusions and the supporting reasoning.

A second *in camera* meeting follows a month or so after the rebuttal hearing. Comments from the parties are reviewed and the factual part of the report is completed. Sometimes the legal conclusions are completed at this third meeting; sometimes it takes longer. When panels consist solely of Geneva-based individuals, this final step in the decision-making process can be broken into a series of shorter and more frequent meetings. When out-of-town panelists are involved, the work tends to be concentrated in one or two follow-up meetings of several days duration, during which a pretty intense work schedule is followed.

The final report is circulated confidentially to the parties. The parties are given a period to explore the possibility of settlement in light of the report. In theory, the consultation period is set by the panel, usually between a week and a month. But in fact, the parties themselves can agree to extend it as long as they wish. If a settlement occurs, the report is torn up and replaced by a brief recital of the facts and the occurrence of a settlement. If no settlement occurs, the report is printed as a restricted GATT document, circulated to all other contracting parties, and placed on the agenda of the next Council meeting.

The panel report itself has no legal standing. Only the Contracting Parties (or the GATT Council acting in its stead) can issue authoritative legal rulings. So, the report must be approved—either as is, or as the Council agrees to modify it. Approval is by consensus, which means the defendant can block it.

It can take anywhere from 10 days to 2 months until the panel report is placed before the first Council meeting. Often the report will be adopted at the first meeting. Sometimes the defendant will request more time to reflect. When this happens the Council usually agrees to defer the matter to a second meeting. The large majority of reports are adopted by the end of the second meeting.

Starting from the moment when a government enters its formal request for creation of a panel, a final report from the panel can rarely be completed in less than four months, and six to nine months would be a more realistic estimate. Approval of the report can add anywhere from 10 days to 3 months to the elapsed time.

Approval and Enforcement of GATT Legal Rulings

Prior to 1976, all GATT panel reports had been approved, except one rather special case in 1956 involving a panel of customs experts interpreting the breadth of a tariff concession. Then, in 1976 the famous DISC reports were handed down. The case involved an EC complaint against a U.S. tax subsidy called DISC, and three U.S. counterclaims alleging that if DISC were a subsidy, so were three European tax laws. The panel found all four measures to be export subsidies inconsistent with GATT obligations. The three European countries said the decisions were wrong and refused to accept them. The United States said it would accept the ruling against its DISC law *only* if the rulings against the three European tax laws were approved at the same time.

The GATT does not really have a formal process for appealing a panel decision. When one party disagrees with the correctness of the panel's conclusions a deadlock ensues. The deadlock is a form of appeal to the rest of the GATT constituency. If the opinions of other GATT governments form a strong consensus in one direction or another, that consensus may be able to beat down the resisting party, thereby resolving the issue. In the DISC case, for example, a consensus emerged that the decision against the three European tax laws was wrong and that the decision against the U.S. law was right. The consensus eventually succeeded in beating down the opposing U.S. view. In 1981, the GATT Council was able to adopt a decision which accepted the three European reports in form, but overruled them in substance; ten months later, the United States agreed to repeal DISC and to substitute a tax law similar to the European laws, a promise that was carried out about two years later.

Since 1980, there have been at least two other panel decisions set aside by the same process. One was a panel report that found certain Spanish restrictions on soybean oil to be consistent with GATT, and the other was a finding that Section 337 of the U.S. trade laws was GATT-legal as applied. In addition, however, there has been an uncomfortable number of panel rulings that have been blocked without any formal resolution. I can count six cases that have remained blocked for some years now, and one or two pending that may be in line for similar treatment. There have been about 40 panel rulings since 1976, so we are talking about almost 20 per cent that have ended in deadlock during this period. While this percentage is clearly larger than anyone wishes, the fact that about 75 per cent of the panel rulings have been routinely approved should be underlined. The process needs improvement, but all things considered, it is still working pretty well as it is.

Where a ruling of violation is approved, the Contracting Parties normally begin by recommending that the offending practice be removed. If the recommendation is not carried out, the Contracting Parties have authority to authorize retaliation, but that sanction has been applied only once – in 1952. Indeed, except for occasional threatening noises, the sanction has been requested that one time only.

In the view of most governments, the only practical sanction GATT can exert in cases of violation is the general diplomatic pressure exerted by calling for reports until something is done. In the 75 per cent more or less routine cases, that pressure has usually been enough. Most of those decisions have brought about enough progress to warrant a claim of victory. It can take a few years, however.

Deadlocked cases have sometimes resulted in one party taking unilateral retaliation, often met with counter-retaliation. But this extralegal warfare is usually limited to symbolic gestures. In deadlocked cases too, the main effecs of GATT legal rulings are the diplomatic pressures they generate. Even here such pressures have some effect. A careful study of GATT's deadlocked cases will show that most follow a twisting path that eventually arrives at a settlement of some sort. Although the disputed GATT rulings have obviously not governed these outcomes, they seem to have functioned something like a dynamite charge thrown into a diplomatic logjam, breaking the impasse enough to allow things to move forward into a somewhat more satisfactory configuration.

The Problems in GATT Dispute Settlement: Lessons for the FTA

1. I would like to begin with two problems that do not usually appear on the roster of GATT's most evident shortcomings. Both are brought to mind by the mention of the DISC case a few moments ago. The first is the vulnerability of GATT dispute settlement procedures to jurisdictional disputes between government agencies. The first U.S. reaction to the DISC case, for example, was to refuse to recognize GATT's competence to discuss it. Why? Because DISC was a law sponsored by the U.S. Treasury Department, and GATT was an international organization that dealt with trade ministry problems. The U.S. Treasury Department did not need the GATT to tell it how to run its international tax policy. This "go to hell" reaction is not easily overcome. It will persist even when jurisdiction is grudgingly admitted. In the DISC case, for example, even after GATT jurisdiction had been established, the Treasury Department refused to cooperate unless the case was processed under a dispute settlement procedure that conformed to its own view of the merits of the case. The unruly behaviour of the U.S.

Treasury Department was one of the reasons why it took 12 years to bring the DISC case to a conclusion.

The lesson is simply this: The efficacy of a dispute settlement procedure depends upon the cooperation of governments, and cooperation in the first instance depends upon the recognition by government agencies of the competence of the procedure. The broader the subject matter of the agreement, the more room there is for jurisdictional border wars. The Canada-U.S. Free Trade Agreement is broader than GATT.

2. The second major problem revealed by the DISC case was the vulnerability of GATT procedures to what might be called inconsistent lawyering. When governments become involved in domestic litigation, there is a structure of decision making whereby government lawyers in charge of the litigation are able to resolve agency differences by insisting that a consistent and coherent legal position be settled upon. GATT dispute settlement often suffers from a want of such internal structures. The problem is that international dispute settlement proceedings tend to have indeterminate legal effects, and this indeterminacy allows political officials to retain control over legal strategy. The result is often a legal position which looks like a candy-store collection of inconsistent or unrealistic political posturings. The absence of coherent legal theories makes the job of any tribunal much harder.

   The general dispute settlement procedures of the Canada-U.S. Free Trade Agreement will have the same need for helpful lawyering. Unfortunately, government legal positions in these proceedings are likely to be subject to the same sort of political control.

3. The most visible problem with GATT dispute settlement today is the difficulty of making it move forward expeditiously. The problem lies partly in the GATT's reliance on consensus decision making, but it is also due to a number of other factors that cause delay even under rigorous time schedules.

   - Bilateral consultations can undoubtedly be slowed by foot-dragging, but delay can also arise from the normal difficulties of scheduling meetings between busy officials. Pushing too hard has its dangers; it is never in a government's interest to let a genuine chance for negotiated settlement go by. Mandatory time schedules will help avoid foot-dragging. Nonetheless, the parties to the FTA will often be forced to choose between speed and more effective consultation.

- In GATT, stalling occurs when the Council is asked to create a panel. The automatic FTA procedure will avoid genuine stalling at this point. Once again, however, there will be times when the complaining government finds it in its interest not to insist on deadlines.
- The FTA will obviously not suffer from GATT's current problem of third-party interference with establishing terms of reference. The FTA procedure may, however, encounter the the GATT's former problem of *party* efforts to tilt terms of reference in their favour. If one of the parties to the FTA should happen to have both a disproportionate share of the power and an easily bruised sense of self-righteousness, some effort to flex its muscles over terms of reference can be anticipated.
- The GATT's largest problem with start-up time at present is panel selection because government litigants are becoming more and more reluctant to accept neutral delegates from other GATT countries as panel members, and the list of outside panelists is not yet well enough established to inspire much confidence. The FTA looks like it has solved this problem with its agreement to establish a list of preselected panelists and to automatic appointment procedures from that list. In all probability, Canada and the United States should not find it difficult in practice to agree to a list of decision makers acceptable to each other. The GATT, by contrast, has virtually no chance of doing so among a 96-country membership.

4. Once panels are in place, there tend to be two major sources of delay in reaching decisions, neither of which the FTA can easily escape, despite its more rigorous time rules.
    - The most frequent source of delay is simply governmental agreement to delay. No matter how much they may decry delay in public meetings, governmental officials usually wince whenever short deadlines are mentioned in their own cases. They are, after all, as overworked as the rest of us, and so tend to accept postponements with alacrity. When the two sides agree the panel has no choice.
    - The GATT has found the use of outside, nongovernmental panelists to be rather cumbersome. The panelists' professional schedules will have to be accommodated, and finding blocks of time large enough to allow for extended meetings and travel time is not easy. Five panelists (the FTA model) will be at least twice as cumbersome as three.

5. The legal quality of GATT panel decisions is still a matter of concern, and this problem will confront the FTA from the outset. The quality of GATT decisions, though significantly better than 10 years ago, continues to depend on the particular composition of the panel, and can also be influenced by the particular Secretariat persons working on the case. The creation of a separate GATT legal staff has made a big difference in establishing a more uniform legal quality, but the legal staff has so far not been large enough to monitor every case carefully, nor does it always find itself working in complete harmony with other Secretariat staff assigned to the panel. Given the fact that most GATT panelists, even those from Geneva delegations, have only occasional contact with GATT legal matters, the Secretariat assistance is in most cases critical. To put it most dramatically, it is my view that the GATT Secretariat could run the dispute settlement machinery without panelists, but most panelists would be lost without the GATT Secretariat.

   The quality of panelists appointed to the FTA lists can be expected to be reasonably good, but they will be strangers to the process. Thus the quality of their decisions will likewise depend to a great extent on the quality of the Secretariat support they get. The text of the FTA itself gives no reason to hope that the FTA Secretariat will provide much assistance. The text suggests that the Secretariat is to be primarily a filing office, staffed by junior officials from the trade ministries in each government. These will be loyal government servants under orders from above, by definition incapable of providing independent legal advice to help panels. *Probably the most critical of all the issues for the FTA dispute settlement machinery will be whether the FTA Secretariat will be allowed to develop beyond this minimalist role.* It would be nice to think that the two governments will have the same capacity for growth and ingenuity as the GATT.

6. The lack of effective sanctions is sometimes cited as a weakness of GATT dispute settlement, but in my view this is a misdirected criticism. While the enforcement pressures at the disposal of the GATT dispute settlement procedure are primarily the normative pressures generated by GATT legal declarations themselves, it is a mistake to treat these enforcement pressures lightly. Declarations made by a respected international institution do have force; the more valued the institution, the more force they have. Each time a government refuses to go along with a legal ruling, it tears a piece out of the institution. Governments do not lightly destroy things they value.

Moreover, I believe that the normative pressures of legal declarations are about the upper limit of the coercive pressures that governments are willing to accept in international institutions. If governments are willing to accept any stronger form of coercion at all, it will be *internal* coercion – the coercion that their own domestic legal systems exert when international norms are enacted as domestic law binding on government officials. Such internal coercion is significantly more powerful, as a day-to-day matter, than most kinds of international coercion one can imagine, but governments nonetheless find it easier to accept because they retain the key to the prison in their own pocket.

In short, the problem with the effectiveness of GATT norms does not lie in the absence of sanctions; it lies in the unwillingness of governments to enact GATT norms into domestic laws. In the long run, the effectiveness of GATT law will depend on what happens in national legislatures.

I would make the same argument concerning the legal force of the Canada-U.S. Free Trade Agreement. In the long run, the force of the Agreement will depend upon the extent to which it can be incorporated into the domestic law of the two countries. In the meanwhile, about all the force that the Agreement itself can provide is the normative force of expert legal decisions, rendered as clearly, as convincingly and as authoritatively as possible.

The FTA seems to belie this prediction by providing for two more muscular kinds of dispute settlement – the Chapter 19 procedure for AD/CVD review and the Chapter 18 procedure for reviewing safeguards measures, both of which provide that tribunal decisions shall have binding effect in national law. The Chapter 19 procedure is a delicate hybrid that owes its existence to the very unusual context of AD/CVD issues in the negotiations; while it is a nice piece of work that can probably achieve its objectives if not taxed too hard or too often, in the long run I feel certain that Chapter 19 will end up hanging from the ceiling of the some legal museum. The "binding" character of the Chapter 18 procedures for safeguards is a surprise. To be honest, I would expect that the implementing legislation on this subject will be extremely narrow or qualified, especially on the general question of "serious injury."

Setting aside this probably ephemeral vision of genuinely binding arbitration, I would argue that the general dispute settlement provisions of the FTA in Chapter 18 do what can be done by focusing on the essential ingredient of first-level legal force – an essentially automatic procedure under which either party can obtain an impartial legal ruling. The Agreement does a pretty good job in this regard, particularly with the panel roster procedure. From here on, the impact of the procedure will depend upon whether administrators will be able to make it work to its full potential – good decisions, high visibility in the defendant country, and as much instant prestige as Madison Avenue can muster. As with the GATT, the creative part of the work has been left to those who administer the Agreement.

7. The GATT's experience with appeals from panel decisions calls attention to one troublesome aspect of the FTA procedure that may well diminish its impact. Claims of "legal error" can deflect a good deal of the normative pressure generated by a legal ruling. Because GATT has not had a very good procedure for handling claims of legal error by losing litigants, those claims of error have been used as a shield in almost all cases where litigants have chosen to resist panel decisions.

   Weak as it may be, however, the GATT procedure does at least have its "court of third-country opinion," which has functioned successfully in the past to beat down a number of spurious claims of error. There are no third countries in a bilateral agreement. As it now stands, therefore, the FTA disputes procedure will be especially vulnerable to claims of legal error.

In my view, one of the priority items in the Uruguay Round agenda for GATT reform should be a better procedure for resolving claims of legal error, preferably an appeal process that governments claiming error could be invited to invoke, albeit with the understanding that they will accept the result. Such a procedure would be even more valuable in the FTA.

Dispute Resolution

Julius Katz

From the outset, I have to say that when I agreed to appear before this panel, I did not know that Bob Hudec would be one of its members. As Frank Stone said, Mr. Hudec is one of the world's great authorities on GATT dispute settlement, if not on international dispute settlement generally. I am therefore in a somewhat unenviable position, saved only by the fact that I speak after he does, so he cannot criticize me. While I have the opportunity to criticize him, there is little with which I disagree.

There are a few points I would like to make. First, in a sense the comparison between the GATT and the FTA is unfair. These are two very different institutions. Bilateral mechanisms are far less complicated than multilateral ones. Furthermore, the United States and Canada have relatively similar approaches to policies, and economic policy is more difficult to manage between countries with very different economic institutions and philosophies.

Secondly, the GATT dispute settlement mechanism has demonstrated very clearly that, however developed and well designed a dispute-resolution mechanism is, it cannot compensate for the absence of agreement on rules. As it turns out, despite the perception that the GATT dispute machinery is seriously defective, on the whole it has worked rather well. Granted, there have been some hard cases, and Mr. Hudec has described the worst ones—namely, the value-added tax cases. There are other recent bad examples dealing with agricultural policy, particularly agricultural subsidies, where the dispute resolution has bogged down (the wheat flour case has been pending since 1981). These cases have been difficult, however, because the GATT rules in these areas are vague or nonexistent. Apart from these cases, the system has worked quite well.

As the GATT has grown, the amount of GATT litigation has grown, and with it problems in the GATT mechanism have become evident. There is, however, a more fundamental problem, that is, the different approach to dispute settlement favoured by many parties to the GATT. Some countries believe that very heavy emphasis should be placed on negotiation and conciliation. While there is likely little controversy over the need to resolve disputes by agreement, where agreement is not possible the United States tends to believe that the matter should be adjudicated promptly. The other countries believe, however, that heavy emphasis should be placed on avoiding litigation or adjudication. At a meeting last year on dispute settlement in the Uruguay Round, it was expressed that, because the GATT was a contract, adjudication should be avoided. It is apparent that the Americans cannot understand this. Nonetheless, the GATT procedures have evolved in such a way as to provide for resort to panel procedures for the adjudication of complaints.

The problem which Mr. Hudec has described with regard to the panel procedure is the focus of the proposals to improve the system which are now being negotiated in the Uruguay Round. I will not speak of other governments' proposals with which I am less familiar. I will say a word about the U.S. proposals, since these have been discussed publicly and because I have been involved with them.

One proposal is that the mediation and conciliation role be clearly set apart from the adjudication procedures, particularly to place that role in the hands of the Director General of the GATT. The procedures presently provide that a party to a dispute can seek the assistance of the Director General. The proposal seeks to mandate that the Director General get in front of a dispute and, if possible, resolve a dispute before it becomes politically difficult.

A second proposal is to introduce the notion of arbitration, which is not currently provided for in GATT procedures. In the GATT, the closest to arbitration was the procedure to settle the U.S.-E.C. chicken war case, which was not described as arbitration although it was clearly handled as such. The GATT is one of the few commercial agreements that does not provide for arbitration.

If a dispute is not resolved by mediation or arbitration, the dispute should then go to a panel for adjudication. U.S. proposals in this area call for clearer rules for the establishment of panels and for the conduct of panel business. Specifically, the United States has proposed greater use of nongovernmental experts, standard terms of reference and time limits for each stage of the panel procedure. The U.S. proposals for improvements of the GATT mechanism are indeed consistent with the procedures incorporated in the FTA.

A major difficulty with the GATT procedures is the requirement that panel reports be adopted by the GATT Council by consensus, since any party to a dispute can block a panel report. To resolve this problem, it was suggested that the parties to a dispute not vote (i.e., consensus minus two). While the United States has not taken a firm stand on this issue, it seems that a better approach would be to have panel reports stand independent of a political vote by the GATT Council.

The enforcement mechanism of the FTA is not different from that of the GATT. The remedy for nonenforcement of a decision by the GATT Contracting Parties is either compensation (i.e., the defendant party offers concessions equal to the damage from its action) or retaliation (the plaintiff party withdraws concessions). The FTA has a somewhat similar provision. In the final analysis, an aggrieved party can abrogate the Agreement, although this would not occur except in most extreme circumstances.

In closing, there is a perception that GATT panel decisions are frequently ignored. In fact, in the vast majority of cases GATT panel decisions are accepted and remedial action is taken. In most cases brought before the GATT, the parties have been able to arrive at a resolution or have implemented decisions called for by panels. It is, of course, the failed cases which gain notoriety.

In summary, if the GATT dispute-resolution mechanism has worked well on the whole, the FTA mechanism should work even better. Many of the improvements presently being sought in the GATT are already incorporated in the FTA. Most important, however, the shared approaches of the United States and Canada as well as the stake each has in making the FTA a success, suggests that both governments will view the dispute-resolution machinery in a constructive rather than adversarial light.

IV.

Trade Laws

The Dispute Settlement Mechanisms of the Canada-U.S. Free Trade Agreement: Comparison with the Existing System

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Debra P. Steger

Introduction

An objective analysis of the dispute settlement mechanisms of the Canada-U.S. Free Trade Agreement (FTA) requires their assessment in comparison to the current system for resolving trade disputes between our two countries as well as to those of other free trade agreements. The current system consists primarily of the General Agreement on Tariffs and Trade (GATT)[1] and domestic Canadian and U.S. trade laws that implement the GATT provisions.

There are several free trade area agreements in effect among industrialized countries in the world, including the U.S.-Israel Free Trade Area Agreement, the Australia-New Zealand Closer Economic Relations Agreement, the European Free Trade Association (EFTA), the former U.K.-Ireland Free Trade Agreement and the agreements between EFTA countries and the European Economic Community (EEC). In addition, there are a number of regional trading arrangements among developing countries such as the Association of South East Asian Nations, the Caribbean Community, the Andean Pact and the Latin American Integration Association.

The FTA mechanisms for dispute settlement are, in several respects, an improvement over the current system for resolving trade disputes. First, the FTA mandates substantial changes to the escape clause or safeguards laws of both countries that are likely to reduce the number of bilateral cases in which measures, such as duties or quantitative restrictions are imposed. Second, the binational panel review mechanism for antidumping and countervailing duty (CVD) cases should reduce the delays and costs of reviewing final investigating agency orders in the courts in the United States and Canada. Third, the commitment to work together to develop and implement a new system of trade laws within a period of five to seven years is an important step both for the Canada-U.S. relationship and for the Uruguay Round of multilateral trade negotiations. Fourth, the establishment of formal channels of communication between the two governments to precede the enactment of new trade legislation or other measures affecting trade, should provide early warning of potential problems and should encourage the two governments to avoid disputes or seek their early resolution. Finally, the establishment of a Canada-U.S. Trade Commission with the power to appoint binding arbitration panels and panels of experts to arbitrate or adjudicate disputes is an important step in Canada-U.S. trade relations.

Although the institutional mechanisms of the FTA are not perfect, they should evolve into a permanent, authoritative binational institution. Designing the institutions to administer a new trade agreement and to resolve disputes that may arise, requires a delicate balance between the objectives of the Agreement and the domestic member governments' concerns about ceding decision-making authority to a new supranational body. Perhaps the institutional provisions of the FTA are the most that the two governments could have agreed to at this point in time.

The FTA, by its nature, is an evolutionary document; some of the rules, for example those in relation to antidumping and countervailing duty laws, intellectual property laws, trade in services, financial services, government procurement and agriculture, will be subject to further negotiations and development. The FTA contains specific bilateral commitments to continue negotiations and to develop new rules in many areas. No international agreement governing a trading relationship of this magnitude could be static. Economic as well as institutional changes require that the rules and institutions be modified over time to meet changing conditions.

Dispute settlement mechanisms are not the most important part of any free trade area agreement; the key feature of an international trade agreement is, of course, its rules. Provisions for the resolution of disputes are necessary, however, to deal with a party's failure to live up to an agreement's terms.

Rule systems are important in international trade because they provide for a measure of predictability and stability in private and public international relations. As John H. Jackson has stated:

> In economic affairs particularly, rules may have a role of greater importance: to facilitate decentralized enterprise decisions such as those concerning investments; to allow a myriad of detailed actions to be taken at lower levels of government officialdom, thus sparing higher authorities; to give governments some argumentative ammunition to counter parochial short term citizen demands which could have a long range damaging effect on the world economy.[2]

For a small country engaged in a major trading relationship with a much larger world power, there are significant benefits to a trade relationship based on a system of rules. The FTA comprises a unique, comprehensive system of rules to govern the Canada-U.S. trading relationship. It also incorporates an institutional framework to monitor that relationship and to avoid and resolve disputes. Moreover, the institutional framework will provide a forum for the development of new rules as required. The mandate of the Canada-United States Trade Commission, established under the FTA, is as follows:

> . . . to supervise the proper implementation of this Agreement, to resolve disputes that may arise over its interpretation and application, to oversee its further elaboration, and to consider any other matter that may affect its operation.[3]

The Dispute Settlement Provisions of the FTA

Two chapters of the FTA are devoted exclusively to dispute settlement: Chapter 18 (Institutional Provisions) and Chapter 19 (Binational Panel Dispute Settlement in Antidumping and Countervailing Duty Cases).

Antidumping and Countervailing Duty Provisions

Canada and the United States have agreed to develop and implement, within a period of five to seven years, a "substitute system" of antidumping and countervailing duty laws. The two countries have agreed to establish a "Working Group" and to use their best efforts to develop and implement the new system within the agreed time. If the new system is not implemented within the five- to seven-year period, either country may terminate the FTA on six month's notice. In the interim, both countries will continue to apply their own AD/CVD laws with the right to change their domestic laws reserved.[4] Each country's right to apply and amend its domestic laws, however, is subject to two important constraints.

Under the FTA, a binational panel procedure will be established to replace the present judicial review of final AD and CVD orders where requested by either member country. The binational panel will be selected, at the request of either country, to review final AD or CVD orders made by either the U.S. Department of Commerce (DOC) or the U.S. International Trade Commission (ITC), the Canadian Department of National Revenue, Customs and Excise (DNR) or the Canadian Import Tribunal (CIT). The panel's task is to determine whether the agency concerned rendered its decision in accordance with domestic law. The panel is required to apply the standard of judicial review applicable in the country where the investigation took place. The panel's decision will be binding on the member countries and their agencies.

If a member country intends to amend its domestic AD or CVD laws, it will be required to name specifically the other country concerned in the proposed legislation and to notify that country of the amendments. The country concerned may request consultations with the country proposing the legislative amendments. Any proposed changes to domestic legislation must be consistent with GATT, the Antidumping and Subsidies Codes, as well as with the object and purpose of the FTA. If government-to-government consultations fail to achieve a resolution, the country concerned may request that a binational panel be appointed to review and issue a declaratory opinion on the proposed amendments. Where the binational panel issues a declaration recommending modifications to the proposed changes, the two governments will be required to enter into compulsory consultations for a period of 90 days during which they are to seek a mutually agreeable solution. If the country proposing the amendments fails to comply with the panel's opinion and, if no mutual resolution is reached within nine months, the country affected by the proposed amendments may enact mirror legislation or terminate the FTA with 60 day's notice.

Institutional Provisions

Elaborate institutional provisions are to be established under the FTA. Although these provisions are modelled on the GATT and the Tokyo Round Codes, there are important differences. Where a formal dispute involving both the GATT and the FTA arises, the dispute settlement provisions of either agreement may be used. Once a country elects to use either the binational or GATT procedures, however, it must use those procedures exclusively.

The FTA institutional provisions involve more than dispute settlement. A Canada-United States Trade Commission (the commission) will be established to supervise the implementation of the FTA, to oversee its further elaboration and to assist in the resolution of disputes. The commission will comprise of representatives from both member countries and will be headed by the cabinet ministers responsible for international trade, or their designees. The commission will have the authority to create subsidiary *ad hoc* standing committees or working groups to assist in the consideration of matters concerning the interpretation or application of the FTA, to investigate and assist in the resolution of disputes, and to negotiate and assist in the development of new rules under the FTA.

Essential to the proper functioning of the FTA are the provisions for notification and consultation. Each member country is required to provide written notice to the other of any actual or proposed legislation, regulation, governmental procedure or practice that might materially affect the operation of the FTA.[5] This includes *any* government measure or action that might affect the object and purpose of the FTA. At the request of the affected country, the notifying member country is required promptly to provide information and to respond to any questions asked. A member country may request consultations with respect to these notifications or any other matter that may affect the operation of the FTA.[6]

Formal channels for government-to-government communication of matters that may affect the Canada-U.S. trading relationship should provide early warning of potential and latent trade problems and should assist either the avoidance or the early resolution of disputes. Under the FTA, Canada and the United States are directed to make every attempt to arrive at mutually satisfactory resolutions through these consultations. If the countries fail to resolve a matter within 30 days of the formal request for consultations, either country may apply in writing to the commission. Unless otherwise agreed, the commission will be required to convene within 10 days to endeavour to resolve the dispute. The commission may use a range of mechanisms in its attempt to reach a mutually satisfactory resolution. It may appoint a special committee or a working group, or it may call on technical advisors or on the assistance of a mediator to achieve a consensus.

Where a dispute has been referred to the commission and there has been no resolution within 30 days, the commission is required upon the request of either country to establish a panel of experts to consider the matter. The commission is required to refer all safeguards disputes, and it may refer any other dispute, to a binding arbitration panel.[7] Where a dispute has not been resolved within 30 days after its referral to the commission, and if the commission has not referred the matter to binding arbitration, the commission, upon the request of either country, is required to establish a panel of experts to consider the matter. There are specific time limits for the establishment of a panel. A panel is deemed to have been established from the date of request. Within three months after the chairman is appointed, a panel is required to present to the member countries an initial report containing its findings of fact, a determination of whether the government measure or action complained of is or would be inconsistent with the obligations of the FTA or would cause nullification or impairment, and its recommendations for resolution of the dispute.[8]

In a safeguards case or any other case which the commission has referred to binding arbitration, the decision of the panel will be final. In other cases, the commission will make a final decision which, in the normal case, would be in conformity with the final panel report. The commission must reach its decision by consensus. If the commission does not reach a decision within 30 days after receiving a final report from a panel, the affected country, where it feels that its rights or benefits are being impaired by the continuation of the measure complained of, may suspend the application of benefits of equivalent effect to the offending country until a resolution is achieved.[9]

Object and Purpose of the FTA

An appreciation for the object and purpose of the FTA is essential to an understanding of how both the antidumping and countervailing duty provisions and the institutional provisions will be applied. In either case, a binational panel is directed to analyze a dispute in terms of the "object and purpose" of the FTA. The general objectives of the FTA, as stated in Article 102, are as follows:

- to eliminate barriers to trade in goods and services between the territories of the parties
- to facilitate conditions of fair competition within the free trade area
- to significantly liberalize conditions for investment within this free trade area
- to establish effective procedures for the joint administration of the Agreement and the resolution of disputes
- to lay the foundation for further bilateral and multilateral cooperation to expand and enhance the benefits of the Agreement.

The object and purpose of the chapter on antidumping and countervailing duty is, in particular, to:

> . . . establish fair and predictable conditions for the progressive liberalization of trade between the two countries while maintaining effective disciplines on unfair trade practices, such object and purpose to be ascertained from the provisions of this Agreement, its preamble and objectives, and the practices of the Parties.[10]

Comparison with the Status Quo

Trade Remedies

Antidumping and Countervailing Duty Provisions

A fundamental provision of the FTA is the U.S. and Canadian commitment to establish a Working Group to develop a substitute system of trade laws for both countries. Canada and the United States have agreed to implement this new system within five years, which may be extended by mutual agreement to seven years. The penalty for not implementing a new system within seven years is potentially serious. Either country may terminate the FTA upon six month's notice.

The proposal to create a new system of trade laws to be administered by a binational commission is not new. The Royal Commission on the Economic Union and Development Prospects for Canada (the Macdonald Commission) recommended in 1985 that a committee of ministers be established to make major decisions concerning the interpretation and implementation of a free trade agreement. it recommended that committee decisions be made by consensus and that a panel of the committee be established to adjudicate disputes involving the enforcement of antidumping, countervailing duty and safeguards laws.[11]

Several experts have recommended that the antidumping laws be abolished and replaced with domestic competition laws.[12] A free trade area, the experts have argued, would essentially eliminate incentives for exporters to dump. If tariffs are reduced to zero, then there would no longer be separate, divisible markets, and competitors in the importing country could simply ship dumped imports back to the exporting country. Some free trade area agreements as well as the EEC Treaty include a "boomerang clause" which guarantees the right to return any exported goods to the country of origin. Guaranteed "reversed dumping" deters exporters from dumping goods into the other member country.[13] Many experts have recommended that in an integrated North American market without tariff barriers, the regulation of discriminatory pricing practices should be left to domestic competition laws. In both Canada and the United States, there are price discrimination and predatory pricing laws to prevent anticompetitive pricing practices from creating competitive distortions in the marketplace.

There are number of proposals concerning government use of subsidies and countermeasures (or countervailing duties) to discipline this. The proposals have ranged from developing a subsidies code to be administered by the existing domestic agencies, to establishing a new binational system for regulating the use of subsidies similar to that in effect under the EEC.[14] No trade expert has seriously recommended that Canadian industries be exempted from U.S. countervailing duty laws. It has long been recognized by economists and trade experts that subsidies can have trade-distorting effects.[15] It is for this reason that the GATT, since its inception, has provided member countries with the right to use countervailing duty measures against subsidized imports from other member countries. Difficulty has arisen over interpretation of the GATT and the Subsidies Code, signed as a result of the Tokyo Round in 1979, because both agreements are ambiguous on the definition of countervailable or prohibited subsidy practices. As a result, the definition and administration of the rules have been left largely to domestic member governments.

Essentially, the Canadian and U.S. laws concerning antidumping and countervailing duties are similar. Canada adopted the *Special Import Measures Act* (SIMA)[16] in 1984 which implemented the 1979 Subsidies Code and Antidumping Code. The United States implemented those Codes in the *Trade Agreements Act* of 1979.[17] Canadian and U.S. agencies responsible for administering AD and CVD laws employ essentially the same substantive standards concerning dumping, subsidization, material injury and causation, although the procedures used and some technical aspects of the calculations differ in some respects. Both Canada and the United States have been relatively active in applying their antidumping and countervailing duty laws against imports from the other country. In the period from 1980 to 1986, there were 31 Canadian antidumping investigations and 1 countervailing duty investigation involving imports from the United States. In the same period, there were 17 U.S. antidumping cases and 13 countervailing duty cases involving imports from Canada.[18] Only a few of these cases have affected large volumes of trade.

The interim procedures established under the FTA to deal with AD and CVD disputes are an improvement over the current domestic trade law systems. The problem Canadian industries have experienced in the past under the U.S. trade remedy system has resulted from the uncertainties caused by the few cases in which political influence appears to have been brought to bear on the determinations of investigating agencies. There have also been progressive attempts by Congress to amend the laws to remedy some of the cases which U.S. interests have lost.[19] The FTA AD and CVD provisions should ensure more predictability and stability in the administration of AD and CVD laws and should reduce the harassment and uncertainty experienced by Canadian firms.

The FTA provisions will affect, first of all, how the United States amends its trade laws. By requiring Congress specifically to name Canada in any legislation designed to affect Canadian industries, the FTA should inhibit Congress from changing AD and CVD laws as they affect Canada. Members of the House of Representatives and the Senate have been extremely reluctant in the past, and in the Omnibus Trade Bill currently in committee conference, to name the specific country targeted by a particular measure.[20] Although many legislative measures proposed in Congress are explicitly protectionist, for the most part senators and congressmen do not wish to be seen as protectionist.

Before the United States amends its trade laws in the future, it will be required to provide written notice and an opportunity for consultation to the Canadian government. At present, there is no formal mechanism requiring the two governments to communicate with each other prior to the enactment of new trade legislation. If consultations fail to achieve a mutually acceptable resolution, Canada may request that a binational panel be formed to consider whether the proposed U.S. legislation is consistent with the GATT, the Antidumping and Subsidies Codes as well as the object and purpose of the FTA. The power of an international body to review proposed legislation and to determine whether it is in accordance with international agreements prior to its enactment, is a unique achievement in international law.

A binational panel appointed in such a case will be required to issue a declaratory opinion, after which both countries are required to consult for a period of 90 days. If the parties do not reach a resolution and if the offending country has not taken measures to comply with the panel's opinion within a period of nine months, the affected country may implement equivalent legislation or may cancel the FTA on 60 day's notice. Under international law, this provision is as binding as decisions of an international body can be; it provides for two stringent methods of retaliation if a country does not abide by the opinion of the panel: the affected country may either implement mirror legislation or terminate the FTA on very short notice.

The panel's procedure for reviewing final AD and CVD orders is a significant improvement over the current domestic trade law systems. First, the procedure will be faster, simpler and cheaper than the current system. Where requested by either country, the binational panels will take the place of judicial review of final orders of the DNR and the CIT in Canada, and the DOC and the ITC in the United States. Currently in Canada, final orders of the CIT may be reviewed by the Federal Court of Appeal under section 28 of the *Federal Court Act*.[21] Federal Court of Appeal decisions may be appealed to the Supreme Court of Canada but they are rarely, if ever, heard. In the United States, final AD or CVD determinations by the DOC or ITC may be reviewed by the Court of International Trade. Its decisions may be appealed to the Court of Appeals for the Federal Circuit, whose decisions may in turn be appealed to the U.S. Supreme Court.

Judicial review of a final CIT order in Canada can take 12 to 14 months. In the United States, two to four years may expire before all legal remedies have been exhausted. The current system is often expensive for Canadian exporters; not only do they have to pay the expenses of litigation, but after an affirmative DOC preliminary determination, they must pay preliminary or provisional duties on any products exported.

The procedures of the binational panel should provide an important commercial benefit to Canadian exporters. They will ensure that a final investigating agency determination is reviewed expeditiously, within a maximum of 315 days measured from the date of publication of the final agency order.[22] Since requests for review and presentation of a case must be made by a member government, the cost to a private firm or firms engaged in a CVD or AD action will be reduced. Currently, Canadian exporters involved in a countervailing duty or antidumping investigation in the United States must bear the full costs of presenting their case before the DOC, the ITC, the Court of International Trade and the Court of Appeals for the Federal Circuit. Also, because of the possibility of legislative amendments by Congress, Canadian firms must plead their case before the staff of Congress and government departments, such as the U.S. Trade Representative (USTR). The proposed binational review procedures under the FTA will make it simpler, cheaper and faster for Canadian exporters to seek review of final U.S. AD or CVD determinations.

Additionally, a binational panel review procedure is likely to result in more predictable determinations in U.S. cases involving Canadian exporters since there will be five panelists deciding a case rather than one judge. Decisions rendered by five panelists are more likely to be consistent with prior decisions than decisions rendered by a single person.[23] The development of a new system of law requires consistency and continuity in the decision making; governments gain confidence in and respect for international bodies acting in a responsible and consistent manner. Ultimately, the efficacy of the FTA dispute settlement mechanism will depend upon the measure of respect that it is able to command from the member governments.

Binational panels will be instructed to apply the same standard of judicial review as that employed in the country where an investigation has taken place. In Canada, a CIT decision may currently be reviewed on the grounds that:

- it failed to observe a principle of natural justice or otherwise acted beyond or refused to exercise its jurisdiction
- it erred in law in making its decision, whether or not the error appears on the face of the record
- it based its decision on an erroneous finding of fact that it made in a perverse or capricious manner or without regard for the material before it.[24]

In the United States, the grounds for judicial review of a final determination of the ITC or the DOC in an AD or CVD case are: whether the decision is unsupported by substantial evidence on the record or is otherwise not in accordance with the law.

The U.S. standard for judicial review of AD and CVD orders is broader than the Canadian standard. As a result, in the last few years the Court of International Trade has overturned or remanded approximately one third of the cases it has reviewed. By contrast, the Federal Court of Appeal has remanded only 4 of the 17 cases it has heard since 1979. In three of the four successful applications, the court determined that there had been a breach of natural justice because of the Antidumping Tribunal's failure to disclose relevant documents to the parties.[25] The fourth application was allowed on the basis that the Antidumping Tribunal had erred in law in making its injury determination.[26] In these four cases, the matter was remitted back to the Antidumping Tribunal for a rehearing. The Federal Court of Appeal has not remanded a case since 1983.

The decision of a binational panel is binding on the member governments and their investigating agencies. The panel may uphold or remand an agency's decision to the relevant investigating agency for action not inconsistent with its decision. This is similar to the current practice employed by the Canadian Federal Court of Appeal and the U.S. Court of International Trade.

The power of binational panels to make binding decisions should have a sobering effect on the investigating agencies. There is a perception in Canada that the decisions of the CIT will never be remanded by the Federal Court of Appeal and the record since 1984 (when the *Special Import Measures Act* came into effect) bears this out.[27] The DOC and the ITC in the United States perceive that their final decisions will not ultimately be overturned by the Court of

Appeals for the Federal Circuit, although the Court of International Trade may remand specific matters back to the agency concerned a number of times.

Although the instances in which the DOC or ITC have been influenced by political considerations are rare (the apparent exception being the 1986 DOC preliminary determination in Softwood Lumber from Canada), the fact that their decisions in the future will be reviewed by binational, independent panels should encourage carefully considered, objective decision making.

Emergency Actions

The emergency actions provisions of the FTA are an improvement over the current safeguards measures applied by the United States or Canada under Article XIX of the GATT. The United States currently acts pursuant to section 201 of the *Trade Act* of 1974,[28] and Canada applies measures pursuant to section 8 of the *Customs Tariff Act*[29] and section 5 of the *Export and Import Permits Act.*[30] Under the FTA, Canada and the United States have agreed to a two-track system for future measures to deal with serious injury caused to a domestic industry by sudden surges in imports.

A special bilateral track has been established to deal with increases in imports caused by the reduction of duties or other concessions made under the FTA. Where imports from the other member country alone constitute a substantial cause of serious injury to a domestic industry, the importing country may suspend the reduction of any duty under the FTA or increase the duty to the lower of the current most-favoured-nation rate or pre-FTA levels. The imposition of relief measures under the bilateral track is limited to a period of three years, may be taken only in the transition period (i.e., until 1998) and may be taken only once for any particular product. The bilateral emergency actions provisions are intended to provide domestic industries with an opportunity to adjust to the reduction of duties and concessions made under the FTA.

Substantial changes affecting global GATT Article XIX actions have also been made under the FTA. Currently, section 201 permits the President to impose measures, such as increased duties or quotas, against imports from all countries where there has been an increase in imports that is causing serious injury or the threat thereof to a domestic industry. The FTA provides that in a section 201 case involving several countries, imports from Canada are to be excluded unless they are *substantial* and *contribute importantly* to the serious injury or threat thereof caused by all imports. Imports from Canada must represent more than 5 to 10 per cent of total imports to be substantial.

These new standards will significantly reduce the number of cases involving imports from several countries in which Canada has been "sideswiped."[31] Where a safeguards measure, i.e., the imposition of a duty or a quota or tariff-rate quota, has been applied on Canadian imports, the measure must not restrict Canadian imports below the trend of imports over a reasonable recent base period with an allowance for growth. Thus, an important limit has been placed on the safeguards measures that may be applied against Canadian imports. This limit should ensure that safeguards measures are used for real adjustment reasons, not as a protectionist device.

The FTA also provides formal procedures for notification and consultation before measures can be taken under either the bilateral or the global tracks.[32] There is an opportunity for either member country to challenge an emergency action measure imposed by the other country under the institutional provisions of the FTA. A decision rendered by a binational panel concerning an emergency measure is binding on the member country that imposed the measure.

Institutional Provisions

The institutional provisions of the FTA are an improvement over the existing system. Currently, Canada and the United States do not have formal, binational procedures for notification and consultations with respect to existing or proposed government measures or actions that may affect trade. Apart from the GATT, there are no formal mechanisms for resolving trade disputes. Although the GATT procedures are being improved, there is considerable opinion that the GATT dispute-resolution procedures are not working effectively because of delays, hesitation on the part of governments to use them, bias resulting from an imbalance of power between disputing parties and the lack of adequate resolution in many cases.[33]

The FTA provisions are superior to the current system because they establish specific procedures for notification and consultation concerning actual or proposed government measures or actions in a much broader range of areas than the GATT currently provides for. Also, strict time limits have been introduced in the FTA at every stage of the dispute settlement process. One of the most important criticisms of the GATT is that the dispute settlement process is often subject to lengthy delays. The 1979 Tokyo Round Codes, including the Subsidies Code and the Antidumping Code, were intended to ameliorate this problem. The dispute settlement procedures under these Codes, however, have rarely been invoked.

The legal effect of a finding by a GATT panel is ambiguous and cannot be considered binding. When a GATT panel has written its opinion, it will refer it to the disputing parties and give them an opportunity to negotiate a mutually acceptable result. If the parties cannot resolve the matter, the report will be made public within the GATT and will be referred to the GATT Council for a ruling. As a result of the consensus decision-making practices of the GATT Council, the opportunities for losing parties (often the U.S. or the EEC) to block the Council's issuance of legal rulings have led to lengthy delays.

The FTA dispute settlement procedures are superior to the GATT procedures in that panels may make binding legal decisions in certain cases. In an emergency action, for example, the decision of an arbitration panel will have binding legal effect on both member countries and their agencies. In other cases, the commission may decide to refer a matter to an arbitration panel on the basis that its decision will be legally binding. In such cases, there is no requirement that a panel decision be forwarded to the commission for final approval. If the commission decides not to invoke the binding arbitration procedure, a decision of a panel of experts will be referred to the commission, which will render a decision by consensus. In such cases, there are explicit time limits placed on the commission during which it must achieve its joint decision, or the injured member country may take retaliatory action.

Achieving the consensus of a commission representing two member countries should require considerably less time and effort than the GATT Council of approximately 50 members. Given that the FTA comprises a bilateral relationship, not a complex multilateral one, the time limits for dispute resolution should ensure that disputes are dealt with in an expeditious and efficient manner. The opportunities for the larger country to wield its political influence, and thus to delay and defeat the process, will be fewer where the legal process for arbitration and adjudication is more formalized and is supervised by a binational commission.

Comparison with Other Free Trade Area Agreements

Antidumping and Countervailing Duty Provisions

In no other free trade area agreement is the power of a member country to take actions under its AD or CVD laws prohibited. In the U.S.-Israel Free Trade Area Agreement of 1985, both countries explicitly retained their ability to impose duties or equivalent measures on the other as permitted under the GATT. As a result of that agreement, Israel agreed to become a signatory to the Antidumping and Subsidies Codes and to eliminate certain export subsidies. The U.S.-Israel Agreement explicitly provides that its general dispute settlement provisions do not apply to AD or CVD cases.[34]

The Convention Establishing the European Free Trade Association, signed in Stockholm in 1960, provides that nothing in it shall prevent any member state from taking action against dumped or subsidized imports consistent with the GATT.[35] The United Kingdom-Ireland Free Trade Area Agreement, in effect prior to the accession of the United Kingdom to the EEC, provided in Article XI that nothing in that agreement would prevent either country from taking action against dumped or subsidized imports consistent with its other international obligations.

The agreement between the EEC and the Kingdom of Sweden provides in Article 25 that either party, if it finds that dumping is taking place in trade with the other party, may take appropriate measures in accordance with the GATT. There are no provisions explicitly relating to countervailing duty measures. Article 23, however, prohibits either party from granting any public aid which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods. Either party may refer such practices to the joint committee, consisting of representatives of the EEC and Sweden. The joint committee may examine the matter and, if appropriate, order elimination of the practice. If the party in question fails to comply with the order, or if the joint committee fails to arrive at an agreement on the matter, the affected party may adopt any safeguards measures it considers necessary to deal with serious difficulties resulting from the practice.

In the Australia-New Zealand Closer Economic Relations Trade Agreement (CERTA), signed in 1983, dumping is defined as inconsistent with the objectives of that agreement. The member states are authorized to levy antidumping duties in cases where the basic GATT requirements have been satisfied. There are, however, specific provisions requiring the investigating member country to give prompt written notice to the exporting country and to afford it the opportunity to request consultations when an investigation has been commenced.[36] Article 16 of the CERTA deals with countervailing duty actions. It provides that a member state may levy countervailing duties on goods imported from the other member state where a decision has been made in accordance with the GATT, the Subsidies Code and the CERTA, and where no mutually acceptable alternative action appears to be available. There are special provisions in the CERTA providing for notification, consultation and expeditious resolution of countervailing duty disputes.

Safeguards Provisions

Most free trade area agreements include specific bilateral track provisions concerning emergency action or safeguards measures. In the U.S.-Israel Agreement, for example, there is a provision requiring consultations before any measure is taken affecting the trade of the other member country. With respect to bilateral safeguards actions which relate solely to a suspension, reduction or elimination of any duty provided for in the free trade area agreement, measures are not to be taken unless serious injury to a domestic industry, substantially caused by imports, results from the concessions made in that agreement. There is also a provision allowing an importing member country to exclude the products of the other member country from any import relief that may be imposed in a global safeguards action where the imports from the other member country are not a significant cause of the injury to the domestic industry.[37] The U.S.-Israel Agreement does not provide the same protection from sideswipe in global cases under section 201 as that contemplated in the FTA.

The Australia-New Zealand CERTA envisages safeguards measures only as a last resort, where no other solution can be found and only during the transition period. The CERTA provides for notification and consultations in an attempt to achieve a mutually acceptable solution to avoid the application of safeguards measures. Where no consensus is achieved, the member state adversely affected may refer the matter to an industry advisory body for investigation, report and recommendation for appropriate action consistent with the CERTA. Safeguards measures may be applied only after consultations have taken place and if no mutually satisfactory solution has been achieved. Wherever possible, the member states are directed not to apply safeguards measures so as to restrict trade. Subsequent to the transition period, where severe material injury or a demonstrable threat thereof arises, a member state may request consultations, but remedial action may be taken only if both countries agree.[38]

Institutional Provisions

The institutional provisions of the FTA are superior to the dispute settlement provisions under any other free trade area agreement. The U.S.-Israel Agreement provides for the establishment of a joint committee, headed by cabinet ministers, to review the general functioning of the agreement, conduct consultations, and review the results of the agreement.[39] Its dispute settlement provisions do not apply to the imposition of antidumping or countervailing duties by a member country.

The U.S.-Israel Agreement's dispute settlement provisions may be invoked only where one party considers that the other party has failed to carry out its obligations under the agreement, that measures taken by the other party severely distort the balance of trade benefits accorded by the agreement or that measures taken by the other party substantially undermine fundamental objectives of the agreement. The two parties are to attempt to achieve a mutually agreeable resolution through government-to-government consultations. If this fails, either party may refer the matter to the joint committee. If referral to the joint committee does not resolve the dispute, either party may refer the matter to a conciliation panel. Conciliation panels are to be composed of three members: one appointed by each member country and the third by the two appointees. The panel is to attempt to assist the member countries in coming to a mutually agreeable resolution of the dispute. If this is not achieved within 3 months, the panel must present the parties with a report containing findings of fact, its determination whether either party has failed to carry out its obligations under the agreement, and a proposal on how to resolve the dispute. The report of the panel is nonbinding. After the panel has presented its report, the affected party is entitled to take any appropriate measure.[40]

There is no permanent ministerial committee established under the Australia-New Zealand CERTA. Ministers are to meet annually to review the general operation of the agreement. There are no formal mechanisms enabling joint resolution of disputes. Opportunities for consultations are built into the substantive provisions of the agreement, but there are no explicit conciliation, mediation, arbitration or adjudication mechanisms. A general review of the operation of the agreement is to be conducted by both member countries in 1988.[41]

The Convention of the European Free Trade Association (EFTA) provides for the establishment of a council comprised of one representative from every member state. The council may set up any committees or advisory bodies necessary in order to carry out its responsibilities. A matter may be referred to the council by a member state where it considers that any benefit conferred on it by the convention or any objective of the EFTA is being frustrated, and where no satisfactory resolution has been reached by the member states concerned. The council may arrange for an examination of the matter, appoint an examining committee, make a recommendation to the member states involved and, if necessary, authorize retaliatory action.[42] In exercising its responsibilities to supervise and provide for the further elaboration of the convention, the council may render binding decisions or merely make recommendations to the member states. Decisions and recommendations of the council must be reached by consensus.[43]

The general dispute settlement provisions of the FTA are superior to other free trade area agreements and the GATT in several respects. First, the FTA contemplates the establishment of a permanent commission to supervise the operation of the FTA, oversee its further elaboration and resolve disputes. Second, the FTA provides that the commission may appoint panels to make binding decisions. Third, there are explicit time limits established at every stage of the dispute-resolution process. This should encourage the expeditious dealing of disputes.

The U.S.-Israel Agreement and the Australia-New Zealand CERTA do not provide for permanent commissions with the power to supervise their operation and further elaboration and with the ability to establish panels to render binding decisions. These agreements provide only for *ad hoc* consultations or conciliation, and the ultimate decision-making power rests with the sovereign member states. The EFTA process, although somewhat more formal, is subject to delays because most decisions, including whether the council will consider a matter, are subject to a consensus vote. Furthermore, there are no specific time deadlines in the EFTA process.

Conclusion

The dispute settlement mechanisms under the FTA represent an important break from the increasing unilateralism in trade disputes between Canada and the United States. The two countries have agreed to develop a common system of trade laws within a period of five to seven years. In the interim, an important set of checks and balances will be established to ensure that domestic trade laws are not changed in ways that would hamper one country's access to the other's market. Furthermore, binational review procedures will be established to provide Canadian exporters involved in U.S. antidumping or countervailing duty cases with more expeditious and less expensive review of final agency orders. The opportunity for binational panels to make binding decisions in antidumping and countervailing duty cases may, in the future, ensure objectivity and fairness in agency determinations and may limit the ability of Congress to apply protectionist trade laws to Canada.

Important substantive provisions for emergency actions should limit the application of safeguards measures in global cases where imports from Canada are not substantial or important contributors to the injury caused or threatened by all imports to a U.S. domestic industry. Explicit procedures requiring notification and consultation before safeguards measures are imposed and providing the affected country the right to seek binding arbitration from a binational panel, should create greater certainty and reduce the threat of safeguards laws being used for protectionist reasons.

The binational commission, established to supervise the operation of the FTA, assist in its further elaboration and resolve disputes, should herald a new era in Canada-U.S. trade relations. Formal channels of communication between governments, to precede legislative initiatives and other actions that may affect trade, will be established where there were none before. The express time limits for every stage of consultation, conciliation, arbitration and dispute adjudication should provide expeditious and effective resolution of disputes at less cost to private firms.

The power of binational panels to make binding decisions in antidumping, countervailing duty and emergency action cases, as well as any other case the commission directs, should provide greater certainty and security of access to the United States market for Canadian exporters.

Notes

1. In our reference to the GATT, we include the Tokyo Round Codes signed in 1979, particularly the Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade (the Antidumping Code) and the Agreement on Interpretation and Application of Articles VI, XVI, and XXIII of the General Agreement on Tariffs and Trade (the Subsidies Code).

2. J.H. Jackson, "Governmental Disputes in International Trade Relations: A Proposal in the Context of GATT" (1979) 13 J. World Trade L. 1 at 2.

3. *Canada-United States Free Trade Agreement* (19 December 1987), art. 1802 (1) [hereinafter FTA.]

4. *Ibid.* at art. 1902.

5. *Ibid.* at art. 1803.

6. *Ibid.* at art. 1804.

7. *Ibid.* at art. 1806(1).

8. *Ibid.* at art. 1807.

9. *Ibid.* at art. 1807(9).

10. *Ibid.* at art. 1902(2)(d)(ii).

11. *Report of the Royal Commission on the Economic Union and Development Prospects for Canada*, vol. 1 (Ottawa: Minister of Supply and Services, 1985) at 320-322.

12. These include J.C. Thomas, "Competition Policy and Canada-United States Trade Liberalization," J. Davidow, "U.S.-Canadian Competition Policy Issues in the Context of a Free Trade Zone," and L.A.W. Hunter, "Canada- United States Trade Negotiations: The Role of Competition Policy" (papers presented at a conference on the Canada-United States Trade Negotiations, sponsored by the University of Ottawa Faculty of Law and Public Affairs International (8-9 May 1986); see also R.G. Lipsey & M.G. Smith, *Taking the Initiative: Canada's Trade Options in a Turbulent World* (Toronto: C.D. Howe Institute, 1985); J. Finlayson & J.C. Thomas, "The Elements of a Canada-United States Free Trade Agreement" (1986) 20 Int'l Lawyer 1307; D.E. Rosenthal, "Antitrust Risks in Abusing the Import Relief Laws" (1982) 14 Swiss Review of Int'l Antitrust L. 31; J.J. Barcelo III, "Antidumping Laws as Barriers to Trade – the United States and the International Antidumping Code" (1971-72) 57 Cornell L.R. 491.

13. R.E. Hudec, "An Approach to Antidumping and Countervailing Duty Laws" in E.R. Fried, F.Stone & P.H. Trezise eds, *Building a Canadian-American Free Trade Area* (Washington: The Brookings Institute, 1987) at 111.

14. See D.P. Steger, "The Impact of U.S. Trade Laws on Canadian Economic Policies" in R.G. Lipsey & M.G. Smith eds, *Policy Harmonization: The Effects of a Canadian American Free Trade Area* (Toronto: C.D. Howe Institute, 1986) at 73; M.G. Smith, C.M. Aho & G.N. Horlick, *Bridging the Gap: Trade Laws in the Canadian-U.S. Negotiations* (Toronto: C.D. Howe Institute, 1987); see also, Finlayson & Thomas, *supra*, note 12; Hudec, *supra*, note 13.

15. G.C. Hufbauer & J. Shelton Erb, *Subsidies in International Trade* (Washington: Institute for International Economics, 1984); J.H. Jackson, "Achieving a Balance in International Trade" (April 1986) Int'l Business Lawyer 124; J.J. Barcelo III, "Subsidies and Countervailing Duties Analysis and Proposal" (1977) 9 L. and Policy in Int'l Business 851.

16. S.C. 1984, c. 25.

17. (1979), Pub. L. No. 96-39, 93 Stat. 144.

18. A.M. Rugman & A.D.M. Anderson, *Administered Protection in America* (Great Britain: Croom Helm, 1987) at 26.

19. The DOC preliminary determination in *Softwood Lumber from Canada* (1986), 51 Fed. Reg. 37453, appears to have been influenced somewhat by political considerations. As a result of a negative final determination by DOC in *Certain Softwood Products from Canada* (1983), 48 Fed. Reg. 24 159, bills were introduced in Congress to amend the definition of countervailable subsidy to expressly include certain natural resource pricing practices (Congressman Bonker's bill, HR 1648, and Congressman Gibbon's bill, HR 2451, were introduced in the 99th Congress, lst Session). The "Shakes and Shingles" case emanated out of the 1983 negative DOC determination in *Certain Softwood Products from Canada*. Disgruntled U.S. producers filed a section 201 petition after losing the 1983 countervailing duty case.

20. In the 1987 Omnibus Trade Bill currently in committee conference in Congress, many of the provisions are explicitly directed at Japan. Among these is the "Gephardt Amendment" that would require the President to retaliate against a country which has an excessive trade surplus if negotiations fail to achieve a reduction in the surplus within a fixed period of time. However, congressmen and senators have been extremely reluctant to expressly name Japan in that bill.

21. *Federal Court Act*, R.S.C. 1970 (2d Supp.), c. 10, s. 28.

22. The deadlines for a binational panel in reviewing a final antidumping or countervailing duty order will be as follows:
    - 30 days for the filing of the complaint
    - 30 days for designation or certification of the administrative record and its filing with the panel
    - 60 days for complainant to file its brief
    - 60 days for the respondent to file its brief
    - 15 days for the filing of reply briefs
    - 15-30 days for the panel to convene to hear oral arguments
    - 90 days for the panel to issue its written decision.

The investigating agency concerned is then required to take action not inconsistent with the decision of the panel, within time limits set by the panel, taking into account the complexity and difficulty of such action (i.e., whether the investigating agency needs to obtain new factual information to take such action). FTA, arts 1904(8) and (14).

23. Current practice before the U.S. Court of International Trade is for cases to be heard by a single judge. Legal interpretations can vary with different judges or even with the same judge in different cases. Single judges of the Court of International Trade have delivered conflicting (and sometimes confusing) decisions on the important issue of "specificity" in determining whether a subsidy is " countervailable" under U.S. law. See *Carlisle Tire & Rubber Co.* v. *United States* (1983), 564 F. Supp. 834 (generally available subsidies are not countervailable); *Bethlehem Steel Corp.* v. *United States* (1984), 590 F. Supp. 1237 (generally available subsidies, except tax measures, are countervailable); *Cabot Corp.* v. *United States* (1985), 620 F. Supp. 722 (specificity test rejected); *PPG Industries Inc.* v. *United States* (1987), 661 F. Supp. 258; *Al Tech Specialty Steel Corp.* v. *United States* (1987), 661 F. Supp. 1206; *Can-Am* v. *United States* (1987), 664 F. Supp. 1444 (all upheld specificity test, declared generally available subsidies to be *not* countervailable).

24. *Federal Court Act*, R.S.C. 1970 (2d Supp.), c. 10, s. 28(1).

25. *Brunswick International (Canada) Ltd.* v. *Antidumping Tribunal* (1979), 1 C.E.R. 327; *Taiwan Footwear Manufacturers Ass'n* v. *Antidumping Tribunal* (1980), 2 C. E. R. 251; *De Vilbiss (Canada) Ltd* v. *Antidumping Tribunal* (1983), 1 F.C. 706.

26. *Noury Chemical Corp. and Minerals & Chemicals* v. *Antidumping Tribunal* (1982), 2 F.C.R. 816.

27. There has been no case since 1983 in which the Federal Court of Appeal has overturned a final order of the CIT, or its precursor, the Antidumping Tribunal.

28. Pub. L. 93-618, title III, s. 2257 et seq.

29. R.S.C. 1970, c. C-41.

30. R.S.C. 1970, c. E-17.

31. The FTA provisions would have prevented Canada from being included in the following section 201 cases where imports from Canada represented less than 5 to 10 per cent of all imports:

    Stainless Steel and Alloy Tool Steel (1983), Inv. No. TA-20148, USITC Pub. 1377; *Mushrooms* (1980), Inv. No. TA-20143, USITC Pub. 1089; *Non-rubber Footwear* (1985), Inv. No. TA-201- 55, USITC Pub. 1717; *Certain Metal Castings* (1986), Inv. No. TA-201-58, USITC Pub. 1849; *Certain Canned Tuna Fish* (1984), Inv. No. TA-201-53, USITC Pub. 1558; *Apple Juice* (1986), Inv. No. TA-201-59, USITC Pub. 1851; *Sugar* (1977), Inv. No. TA-201-16, USITC Pub. 807; *Television Receivers, Color and Monochrome, Assembled and Non-Assembled, Finished or Not Finished, and Subassemblies there* (1977), Inv. No. TA-201-19, USITC Pub. 808.

32. A major complaint made by the Government of Canada in the 1986 Shakes and Shingles case was that the President did not notify or consult with the Prime Minister before he imposed the 35 per cent duty. (*Western Red Cedar Shakes and Shingles* (1986), Import Relief Determination, 51 Fed. Reg. 19 157.) Under the FTA, the United States would be required to notify and provide Canada with an opportunity to request consultations *prior* to any action being taken. Also, Canada would have the right to appeal any such decision to a binding arbitration panel established by the Canada-U.S. Trade Commission.

33. J.H. Jackson, "Governmental Disputes in International Trade Relations: A Proposal in the Context of the GATT" (1979) 13 J. World Trade L. 1 at 4-8; J.H. Jackson, "The Crumbling Institutions of International Trade" (1978) 12 J. World Trade L. 93; R.E. Hudec, "GATT Dispute Settlement After the Tokyo Round: An Unfinished Business" (1980) 13 Cornell Int'l L.J. 145.

34. *United States-Israel Free Trade Area Agreement* (22 April 1985) at art. 19.

35. *Convention Establishing the European Free Trade Association* (7 January 1960) at art. 17.

36. *Australia-New Zealand Closer Economic Relations – Trade Agreement* (28 March 1983) at art. 15.

37. *United States-Israel Free Trade Area Agreement*, art. 5.

38. *Australia-New Zealand Closer Economic Relations – Trade Agreement*, art. 17.
39. *United States-Israel Free Trade Area Agreement*, arts 17 and 18.
40. *Ibid.* at art. 19.
41. *Australia-New Zealand Closer Economic Relations – Trade Agreement*, art. 22.
42. *Convention Establishing the European Free Trade Association*, art. 31.
43. *Ibid.* at art. 32.

Dispute Settlement Provisions on Antidumping and Countervailing Duty Cases in the Canada-U.S. Free Trade Agreement

Shirley A. Coffield

The antidumping (AD) and countervailing duty (CVD) dispute settlement provisions have become the most discussed of the Canada-U.S. Free Trade Agreement (FTA).

A major goal of the Government of Canada was to establish a system of binational review of "unfair" trade cases in the expectation that so-called "harassment" cases would be reduced. This goal was fueled primarily by the U.S. decision in the CVD case, *Softwood Lumber from Canada*.[1] While the initial position of the Canadian Government was to have binding binational review early in a domestic procedure, in the final analysis, opposition by the United States led the parties to develop a fairly new and novel system of *ex post facto*, but binding, review of final decisions in lieu of domestic judicial review procedures in both countries.

It is important to note that the present system is intended to be transitional (in effect no more than seven years), while the parties grapple with the larger and more difficult problem of the substantive rules concerning subsidization and use of CVD and AD laws. If successful, this substantive effort will address some of the more concrete issues between the two countries, such as differing programs and philosophies concerning economic development. In the current political context, however, such an undertaking proved to be impossible in the course of negotiations on the FTA. The parties, therefore, focused almost entirely on the judicial and procedural elements of a binational dispute settlement mechanism. Each country retained its current domestic AD and CVD provisions. The binational review simply looks at final decisions made under each country's domestic law and passes judgment on whether those decisions were in conformity with the *domestic* law, albeit recognizing that the domestic law is a reflection of commitments made multilaterally by both parties under the Subsidies[2] and Antidumping Duty[3] codes of the General Agreement on Tariffs and Trade (GATT). The decision of the binational review panel then becomes "binding" on the parties.

Since the FTA details were made public, there has been much discussion about whether the dispute settlement mechanism for CVD and AD cases provides a benefit to Canada. Questions have been raised whether the provisions will actually reduce the number of cases or bring discipline into U.S. policy decisions in sensitive political cases, such as the recent *Softwood Lumber* case.

The dispute settlement provisions do, in fact, make some fairly important changes in the way both countries approach dispute settlement on issues involving specific substantive and procedural laws. Most important, the agreement on *ex post facto* review, and the substitution of the judicial system in each country, leaps the psychological barrier to allow scrutiny of final administrative decisions and binding judgments by binational tribunals. While there have been some cases in which the United States has bound itself to binational tribunal decisions, these have been discreet and limited, and they have not involved the broad and politically contentious areas of international trade and the enforcement of existing U.S. anti-dumping and countervailing duty laws.

Binational review, even *ex post facto*, affects the entire decision-making process from the beginning of any particular case. It affects the decisions of private parties to seek a settlement and as well as the decision of governments to agree to a settlement. It affects the potential for a "deal" which may go beyond settlements provided for by statute. It is likely to have a major impact on whether cases are brought and, if brought, how they are managed. The sum of all the provisions in Chapter 19, then, add up to a great deal more than the mere language that chapter would imply.

The provisions of Chapter 19, including commentary, follow:

Article 1901

This article makes it clear that the dispute settlement provisions apply to *goods* only, as determined by the competent investigating authority. It will be interesting to see how the parties treat the borderline commodities, such as electricity, which is included in the

Harmonized System classification, but which, historically, has not been considered a product for purposes of U.S. trade laws.

Article 1902

This article reserves the right of each party to apply its own AD and CVD laws, and defines those laws as including the relevant statutes, legislative history, regulations, administrative practice and judicial precedents.

This article also includes the so-called "watchdog" provision, which requires that any amendments made by either party to its relevant laws will apply to the other party only if it is specified as such in the amending statute, there is appropriate notification in advance and there is an opportunity for consultation. In addition, amendments must not be inconsistent with the GATT Antidumping or Subsidies codes, or (more vaguely) the "object and purpose of this Agreement and this Chapter which is to establish fair and predictable conditions for the progressive liberalization of trade between the two countries while maintaining effective disciplines on unfair trade practices." This flowery language appears crafted to give a complaining party the ability to gripe whenever anything is changed which has not been agreed to—quite apart from whether or not it has been "litigated" in the GATT, the AD/CVD codes of which are themselves fairly vague and amorphous.

Article 1903

This article provides a mechanism for watchdog panel review and declaratory opinions on potential or enacted (after the FTA implementation) statutory amendments to AD/CVD laws, including the related judicial review and standing. Declaratory opinions of a panel are limited to whether amendments conform to the GATT or the FTA, or whether the amendment overturns a prior decision of a panel *and* does not conform to the GATT and the object and purpose of the FTA. If the watchdog panel proposes changes to any statutory amendment, consultations are required, and if there is no corrective action by the party found at fault, there is provision for legislative or executive action or the termination of the FTA.

Panel procedures under this article set fairly stringent deadlines for panel decisions, with an initial declaratory written opinion due within 90 days after a chairman is appointed. If there is no declared objection within 14 days, the opinion becomes final. If there is an objection, then a final report is due 30 days after the panel hears all views of the parties. Unless otherwise agreed, the deliberations of this panel will be confidential.

Article 1904

This is the major section dealing with review by a binational panel of final AD and CVD determinations. The review is to be on the "administrative record," and the standard of review and general legal principles used must conform to what the country taking action would have applied in its determinations. The language of the provision sounds a great deal more precise than it is given, in the United States at least, in the wide variation of court decisions.

Elements of the Binational Panels

The request for a panel must be made within 30 days of publication of a final decision.

In order for there to be a review, one of the parties must request it. A party must seek review if requested to do so by a dissatisfied domestic private party who would have standing to bring a case. This provides minimum flexibility for a government to turn down a request from a domestic party based on standing.

There is a right of appearance, not only by representatives of the government making the final determination, but by other interested private parties otherwise having standing, who may appear and be represented by counsel.

The panel may uphold a final determination or remand it for changes consistent with the panel's decision. Importantly, the decision of the panel is binding on the parties. The FTA does not affect the judicial review procedures of either party or cases appealed under those procedures with respect to *nonfinal* determinations. With respect to final determinations, however, *if either party requests a panel*, the final determination cannot then be subject to judicial review in either country.

There is a situation, however, in which final determinations could, in fact, go into the judicial review process in the courts of the country involved. The dispute settlement mechanism does not apply where neither party seeks a panel review of a final determination. One can assume that in most affirmative determinations, and in all that would be contentious, the disadvantaged party would seek a review of a final determination. Where there has been a negative determination, however, one would not ordinarily expect the party who " won" (a negative resulted in no action taken) to seek a review. Likewise, at least with respect to the United States, it is unlikely that a private petitioner who has received a negative final determination would seek review of the binational panel. Instead, it is more likely that a U.S. petitioner would not ask for a panel review, wait for the 30 days to expire within which time such a review could be requested, and then seek review in the U.S. courts. However, the FTA provisions ensure that such an action would not be "sprung" on the parties by requiring, as a condition of judicial review, that the party or other person intending to seek judicial review give notice no later than 10 days before the 30-day period within which to seek panel review has expired, thus providing time for the winning party to request a review. Therefore, to ensure that a contentious negative would be reviewed by the binational panel, the anomalous situation arises wherein the winning party might have to request the binational panel to review its victory.

The provisions limiting judicial review apply to decisions made after the FTA goes into effect only. They do not apply to those cases which have resulted from judicial review in the original determination by the court of the importing country, or to final determinations issued as a result of judicial review commenced before the FTA went into force.

Procedures for the Establishment of Binational Review Panels

The provisions for the establishment of a panel contain a number of the usual bilateral and multilateral dispute settlement procedures governing the selection of panelists and the operation of the panel:

1. The roster from which panelists will be chosen will include 50 candidates, 25 chosen by each government from amongst their citizens. No one on the roster may be affiliated with either party (in the employ of the government).
2. The majority of the panelists on each panel must be lawyers.
3. The first four panelists must be chosen within 30 days of a request, each party choosing two panelists. The panelists need not be appointed from the roster but should "normally" be from the roster. Also, as contrasted to the provisions in Chapter 18 (General Dispute Settlement), a party need not select its own citizens for any particular panel but may choose from any name on the roster. Four peremptory challenges are allowed on each side, and another 15 days beyond the 30 is allowed to select alternative panelists. If a party fails to appoint its members within the 30- or 45-day period, they will be selected by lot. A fifth panelist is to be chosen within 55 days of the request for a panel, generally by agreement between the parties, or if there is

no agreement, from the roster. The process could take a possible 61 days.

4. The chairman is chosen by the panelists and must be a lawyer.
5. Decisions of the panel are by majority vote based on votes of all members. The panel must issue written decisions with reasons together with dissenting and concurring opinions of panelists.
6. A code of conduct must be established by the parties with respect to the panel. There must be provisions for protective orders and sanctions for violations of protective orders.
7. Other provisions affecting panelists include: a suspension of proceedings in instances where a new panelist must be chosen; a provision that panelists, to the extent it does not interfere with their panel duties, may engage in other business; a provision that a panelist may not appear as counsel before a panel; a provision that panelists will be immune from suit and legal process related to acts performed by them in their official capacity (with the exception of violations of protective orders or undertakings); and finally, a provision for remuneration of panelists.

Time limits for the panel procedures provide for fairly rapid determinations, especially important in *ex post facto* cases where there has been an affirmative preliminary which would require a bond. Decisions are, in most instances, to be rendered within 315 days of the date on which a request for a panel is made.

All these provisions are fairly stock and provide in a fairly detailed manner for smooth running in the selection and operation of a panel in any particular case.

Extraordinary Challenge Committee

An extraordinary challenge procedure has been established in order to give further appellate review in cases of gross misconduct, bias or serious conflict of interest on the part of a panel which has affected the integrity of the process. The committee is to be comprised of three members who must be judges or former judges in the United States or Canada. A roster of 10 names, 5 chosen by each government, is to be established. For the panel itself, a review can be requested by one of the governments only. Each party chooses one member and those members would then select the third from the roster, or if there is no agreement, the third will be chosen from the roster by lot. Decisions of the extraordinary challenge committee will normally be made within 30 days and will be binding. In case a violation is found, the original panel decision is vacated or remanded to the original panel. If vacated, a new panel is chosen.

Under the provisions of Article 1904, the parties are to adopt detailed rules of procedure for the panels by January 1, 1989. The FTA gives detailed guidance as to the matters to be covered in those rules which are, "where appropriate," to be based on judicial rules of appellate procedure.

Finally, Article 1904 requires the governments to amend their statutes and regulations to conform to the requirements of the dispute settlement provisions. Article 1904 sets out in some detail the laws of both countries to be amended to reflect the agreement between them.

Article 1905

This article deals with the prospective application of the dispute settlement mechanism, making it clear that it applies only with respect to final determinations made after the entry into force of the FTA. With respect to the watchdog legislative provisions, it applies only to those amendments to AD or CVD statutes enacted after the entry into force of the FTA.

Under this prospective application provision, cases in which final determinations were issued prior to January 1, 1989 are not subject to binational review. However, when those cases come up for review in the administrative procedure of either country (in the United States, normally completed at the end of two years), the final determination in any review investigation is subject to the provisions of binational dispute settlement.

A more difficult problem involves provisions in the current Omnibus Trade Bill. The language of Article 1905 makes it clear that the watchdog provision would not apply to any amendments to the CVD/AD laws enacted before January 1, 1989. However, the standstill provision of the FTA, while only hortatory, certainly provides some leverage in that any changes to U.S. law which would greatly affect the intent of the parties should be subject to consultation and discussion. Finally, the provision provides justification for the offended party not to sign the FTA.

Articles 1906 and 1907

These articles establish the goal of developing substantive rules on CVD and AD laws within five to seven years. In addition, a working group is established to discuss rules and disciplines on government subsidies with the goal to develop and implement a substitute system of subsidy rules within the five- to seven-year period which serves as the transition to a new system.

Articles 1908, 1909 and 1910

These articles establish procedures requiring the designation of officials responsible for consultations; establish a Secretariat in each country, including operational details; and finally, provide that a code of conduct be established for panelists and members of committees by the date that the FTA goes into force.

Article 1911

This article defines the various concepts found in Chapter 19.

1. *Administrative record* is defined in some detail. Since the panel standard is review on the administrative record, it is important to spell out what the record is. The record includes all documentary or other information presented to or obtained by the investigating authority in the course of an administrative proceeding. This is an important provision in that it establishes what information is looked at by the panel. While the language is the same as that in the U.S. statute, the practice of the Department of Commerce does not appear to be incorporated into the FTA. Currently, there are instances where information is presented to the Department of Commerce which that department does not accept and which does not, therefore, become a part of the record which is transmitted to the U.S. court for review. A party would have to petition the U.S. court to have certain information included (not often granted, as the court gives great weight to administrative discretion in this area). The FTA provision, however, should not necessarily carry forward the Department of Commerce practice, and a panel is not likely to give the same degree of latitude to the Department of Commerce in limiting the record on matters which may affect its substantive review of a case. Certainly one can read the provision as requiring that *any* information presented by interested parties is sent to the panel for review, whether or not it would have been considered by the Department of Commerce to be properly included in the record (except for irrelevant information, the determination of which should also be reviewable by the panel). The record also includes, as one might expect, the final determination, the reasons for the determination, the transcripts or records of conferences or hearings, and all published notices.

2. *Statutes* are defined specifically to include cited statutes of each country, as well as any successor statutes:
   - *Antidumping* statute, as referred to in Articles 1902 and 1903, means: (1) in the case of Canada, the relevant provisions of the *Special Import Measures Act*, as amended, (2) in the case of the United States, the relevant provisions of Title VII of the *Tariff Act* of 1930, as amended, and (3) the provisions of any other statute that provide for judicial review of final determinations or indicate the standard of review to be applied.
   - *Countervailing duty* statute, as referred to in Articles 1902 and 1903, means: (1) in the case of Canada, the relevant provisions of the *Special Import Measures Act*, as amended, (2) in the case of the United States, section 303 and the relevant provisions of Title VII of the *Tariff Act* of 1930, as amended, and (3) the provisions of any other statute that provide for judicial review of final determinations or indicate the standard of review to be applied.
3. *Competent Investigating Authorities* are spelled out for both countries, for example, the U.S. Department of Commerce and the U.S. International Trade Commission, the Canadian Import Tribunal and the Canadian Department of National Revenue, and their successors.
4. *Final determination* is clearly defined for both countries and includes final determinations to take actions or determinations not to take actions, determinations resulting from reviews or determinations not to institute reviews. In the case of the United States, *final determination* includes a decision whether a particular type of merchandise is within the class or kind of merchandise described in an existing finding of dumping or an AD/CVD order.
5. Further, Article 1911 gives a rather standard definition for *general legal principles* to include standing, due process, rules of statutory construction, mootness, and exhaustion of administrative remedies, and it clearly defines a *remand* as a referral back for determinations not inconsistent with the panel or committee decision.
6. Finally, the *standard of review*, which may be amended from time to time, is defined rather specifically in the case of both countries. With respect to Canada, it is the grounds set forth in section 28(1) of the *Federal Court Act* with respect to all final determinations. In the case of the United States, it is the standard set forth in section 516A(b)(l)(B) of the *Tariff Act* of

1930, except that with respect to determinations by the U.S. International Trade Commission not to initiate a review, the standard is in section 516A(b)(l)(A) of the *Tariff Act* of 1930. The importance of the standard of review is highlighted by the fact that it is specifically defined as part of the AD/CVD statutes. Therefore, while amendments are possible, any material limitation on the standard of review in proposed legislation would trigger the watchdog panel procedure of Article 1903 as being inconsistent with the intent of the FTA.

Conclusion

Some of the critical elements of this dispute settlement mechanism include (1) its binding nature, (2) the standard of review that the panel must use in its determination, (3) the makeup of the panel, and (4) the overall effect of the mechanism on administrative procedures and petitioner decisions with respect to filing AD/CVD cases.

Certainly, we will not know until this provision has been used how the elements cited above will work, how they will interact and what impact this chapter will have on cases filed in each country. One can expect a certain amount of disagreement, misunderstanding and a shaking-out period where this mechanism is sorely tested and subject to political pressure and revisionist thinking on the part of both governments.

It seems clear, however, that a major impediment between the United States and Canada has been overcome by the agreement to establish a binational review panel of a binding nature which will scrutinize the administrative procedures in each country for consistency within domestic law, and as interpreted through multilateral commitments. It seems almost certain that the U.S. Department of Commerce will look more carefully at precedents in cases involving Canada, that policy decisions similar to those made in the *Softwood Lumber* case would likely not be made, and that there will be more awareness of, and an attempt to be consistent with, obligations undertaken in the GATT. The dispute settlement mechanisms allow the Article 1903 watchdog panel and the Article 1904 panel to determine the consistency of proposed statutory amendments and administrative procedures with the multilateral commitments of both parties. Under the theory of the FTA, the legislation and regulations reflect each party's compliance with multilateral commitments. Clearly a panel can exercise a great deal of latitude in interpreting these multilateral commitments, especially since the GATT Contracting Parties have not themselves clearly interpreted many of the relevant code provisions.

In addition, the standard of review under Chapter 19 provides a certain amount of flexibility with respect to the panel's ability and authority to step into the shoes of the competent forum of judicial review in each country. With respect to the United States, that flexibility becomes quite broad and can provide any panel with the ability to distinguish cases and facts and, by so doing, to reach conclusions different from those a particular court may have reached in the past in different, but similar, cases.

Because of the increased flexibility and lack of certainty regarding how any panel might view a particular case, the discipline on the two governments will be increased. In addition, these same factors can be expected to reduce the number of cases which are marginal, which are brought for harassment purposes and which rely upon political pressure to achieve policy changes aimed at achieving results different from those which might have been made under a more conservative application of the law.

There will, no doubt, be contentious cases between these two countries. This mechanism, however, can be expected to lessen the distrust surrounding the decision-making process in both countries. The process will be removed from the purely domestic and, some might say, highly politicized context of an administrative procedure by elevating contentious cases to objective, binational scrutiny. In fact, these provisions are not intended to stop legitimate cases brought against unfair trade practices which are understood by both countries to be in violation of both multilateral and unilateral commitments.

The more difficult task lies ahead, however, when the substantive rules affecting subsidies and CVD/AD statutes are addressed in an attempt to come to some accommodation in the contentious areas of development policy, an accommodation that becomes more crucial with each passing year as the economies of the two countries become even more interdependent as a result of the overall impact of the Free Trade Agreement.

Notes

1. Preliminary CVD Determination: *Softwood Lumber from Canada* (1986), 51 Fed. Reg. 37 453.

2. *Agreement on Interpretation and Application of Articles VI, XVI and XXIII of the General Agreement on Tariffs and Trade* (relating to subsidies and countervailing measures), GATT Doc. MTN/NTM/W/236, reprinted in H.R. Doc. No. 153, 96th Cong. 1st Sess., pt. 1 (1979) at 257.

3. *Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade* (relating to antidumping measures) GATT Doc. MTN/NTM/232, reprinted in H.R. Doc. No. 153, 96th Cong. lst Sess., pt. 1 (1979) at 309, 311.

Antidumping and Countervailing Duty Provisions: Judicial Review by Binational Panels

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Richard G. Dearden

Introduction

The Canada-U.S. Free Trade Agreement (FTA) has created binational panels to judicially review final antidumping (AD) and countervailing duty (CVD) determinations rendered in Canada and the United States (Article 1904(1)). The binational panels will replace the current system of judicial review of final determinations made by the Canadian Department of National Revenue, the U.S. Department of Commerce, the Canadian Import Tribunal and the U.S. International Trade Commission. The binational panels will review final determinations made after January 1, 1989 only (Article 1905).

The Synopsis issued by the Canadian government states: (1) the binational panels are a unique dispute settlement mechanism that will guarantee the impartial application of Canadian and American AD and CVD laws, (2) the binational panels will determine whether Canada-U.S. AD and CVD laws were applied correctly and fairly, (3) the decisions of the binational panels are binding on both governments, and (4) the creation of the binational panel mechanism will create predictability and security of access for Canadian exporters of goods to the United States (*Canada-United States Free Trade Agreement*, "Synopsis" (10 December 1987)).

This paper focuses on the role of judicial review of the binational panels and in particular, the standard of review to be applied by the binational panels, the establishment of the panels and the procedures to be adopted by them.

Standard of Review

Introduction

Judicial review of final AD and CVD determinations requires that the binational panels apply the "standard of review" and the "general legal principles" that would otherwise be applied by a court of the importing party (Article 1904(3)).

In Canada, the standard of review, as may be amended from time to time, are the grounds set forth in section 28(1) of the *Federal Court Act*. These grounds are: (1) the failure to observe a principle of natural justice or otherwise acting beyond or refusing to exercise its jurisdiction, (2) an error in law in making its decision or order, whether or not the error appears on the face of the record, or (3) basing a decision or order on an erroneous finding of fact that is made in a perverse or capricious manner or without regard for the material before it.

In the United States, the standard of review, as may be amended from time to time, is: whether the decision was arbitrary, capricious, an abuse of discretion, or unsupported by substantial evidence on the record; or otherwise not in accordance with the law.

General legal principles are defined as "principles such as standing, due process, rules of statutory construction, mootness, and exhaustion of administrative remedies" (Article 1911).

Grounds for Judicial Review - Canada[1]

Failure to Observe a Principle of Natural Justice

In *Administrative Law and Practice* (2d ed. by R.F. Reid & H. David (Toronto: Butterworths, 1978)), natural justice is defined as "fair play, nothing more." The concept of natural justice is essentially procedural involving (1) the duty to give persons affected by a decision a reasonable opportunity to present their case, and (2) the duty to listen fairly to both sides and to reach a decision untainted by bias.

It is the duty of the Canadian Import Tribunal (formerly the Antidumping Tribunal) to give persons sufficient knowledge of the accusation, arguments and evidence to be considered in support of the accusation against them in order to allow them a fair opportunity to answer anything contrary to their interest, and to make submissions with regard to the material on which the tribunal proposes to make its decision before such a decision is made. This has been considered in the following cases: *Sarco Canada Ltd.* v. *Antidumping Tribunal*

(1978), [1979] 1 F.C. 247 (A.D.); *Brunswick International (Canada) Ltd.* v. *Antidumping Tribunal* (1979), 35 N.R. 71 (F.C.A.D.); *Magnasonic Canada Ltd.* v. *Antidumping Tribunal* (1972), [1972] F.C. 1239 (A.D.).

The Canadian Import Tribunal is under no duty to take active steps to permit the parties to test the accuracy of the information, such as making all the authors of the confidential information available for cross examination (*Re Antidumping Act and Re-Hearing of Decision A-16-77* (1979), [1980] 1 F.C. 233 (A.D.)).

In *Toshiba Corp.* v. *Antidumping Tribunal* (1984), 6 C.E.R. 258, the Federal Court of Appeal held that preliminary reports prepared by the staff of the Canadian Import Tribunal containing a number of statements of fact relating to the issue for decision, should generally be revealed to the parties and that refusal to do so would amount to a technical breach of the rules of natural justice. Preliminary staff reports are routinely disclosed to counsel today. Final staff reports, consisting only of the summary and commentary on the evidence and submissions made at the inquiry, need not, however, be revealed to the parties in order to comply with the rules of natural justice.

Failure by the Canadian Import Tribunal to make a ruling on the scope of its inquiry (i.e., a question raised about the meaning of words contained in the Deputy Minister's preliminary determination) may deprive the parties of the opportunity to lead evidence, not only concerning the class of goods subsequently found to be at issue, but to controvert, correct or comment on the evidence or information relevant to the tribunal's finding (*De Vilbiss (Canada) Ltd* v. *Antidumping Tribunal* (1982), 4 C.E.R. 245 (F.C.A.D.)).

In addition, natural justice includes the duty to adjourn proceedings if the refusal to do so would deny the person concerned a reasonable opportunity to be heard (*Sarco Canada Ltd.* v. *Antidumping Tribunal, supra*).

Otherwise Acting Beyond or Refusing to Exercise its Jurisdiction

There are several types of jurisdictional error. Essentially, these can be divided into the following categories:

- Errors of preliminary jurisdictional fact or law with respect to the tribunal's definition of the scope and parameters of its jurisdiction, resulting in its acting beyond or refusing to exercise its proper statutory jurisdiction. Such errors generally involve mistakes pertaining to the character and composition of the tribunal, the nature of the subject matter of the inquiry and the fulfillment of conditions precedent to the conduct of the inquiry. Although jurisdictional questions are reviewable, the courts have been reluctant to reverse them other than on very strong grounds. See *Cutters Laboratories*

International v. *Antidumping Tribunal* (1975), [1976] 1 F.C. 446 (A.D.); *Sarco Canada Ltd.* v. *Antidumping Tribunal, supra; Brunswick International (Canada) Ltd.* v. *Antidumping Tribunal, supra.*

- Situations in which the authorizing statute is *ultra vires*.
- An invalid appointment of the tribunal.
- Decisions of fact not supported by the evidence.
- The failure to meet express mandatory (as opposed to directory) procedural requirements.
- The denial of natural justice resulting in loss of jurisdiction.
- Exceeding limitations of powers of decision.
- Decisions based on wrong principles.
- A invalid delegation by the tribunal.
- Fraud.
- Decisions that are so unreasonable as to result in the loss of jurisdiction.

The fact that the tribunal could have made a more thorough inquiry does not mean that it refused to exercise its jurisdiction within the meaning of section 28(1)(a) of the *Federal Court Act*. It has been suggested that a challenge under section 28(1)(a) of the *Federal Court Act* could be based on additional evidence led, with leave of the court, as well as evidence on the record as made before the tribunal (*Rohm & Haas Canada Ltd.* v. *Antidumping Tribunal* (1978), 22 N.R. 175 (F.C.A.D.)).

Error of Law

Under section 28(1)(b) of the *Federal Court Act*, all errors of law are reviewable by the Federal Court of Appeal, for example: (1) the misconstruction of statutory provisions, (2) the application of an incorrect onus of proof, and (3) the wrongful admission of evidence and wrongful refusal to hear evidence. With regard to the latter, it would appear that if the tribunal admits the evidence in question, it will not commit an error of law if it gives it inappropriate weight. In *PPG Industries Ltd.* v. *Antidumping Tribunal* (1978), 22 N.R. 263 (F.C.A.D.), an applicant for review under section 28 claimed that the tribunal had failed to take into account or give any weight to certain oral and documentary evidence and that, if it had, it could not have reached the conclusion respecting material injury that it did. The court refused the application on the grounds that, because the tribunal had weighed the evidence, any interference by the court would amount to retrying the case by giving to the various pieces of evidence the weight which the applicant submitted to be proper (see also *Merkuria Foreign Trade Corp.* v. *Antidumping Tribunal* (1980), 2 C.E.R. 142 (F.C.A.D.)).

In some circumstances, errors of fact may amount to errors of law. For example, in *Canadian Lift Truck Co.* v. *Deputy Minister of National Revenue for Customs and Excise* (1955), [1956] I D.L.R. (2d) 497 at 498, the Supreme Court of Canada held (per Kellock J.):

> While the construction of a statutory enactment is a question of law, and a question as to whether a particular matter or thing is of such a nature or kind as to fall within the legal definition is a question of fact, nevertheless if it appears either to the appellate Court that the tribunal of fact had acted without any evidence or that no person, properly instructed as to the law and acting judicially, could have reached the particular determination, the Court may proceed on the assumption that a misconception of law has been responsible for the determination.

It appears that, *prima facie*, a challenge under section 28(1)(b) of the *Federal Court Act* requires reference only to the record as made before the tribunal (*Rohm & Haas Canada Ltd.* v. *Antidumping Tribunal, supra*).

Erroneous Finding of Fact

In *Re Antidumping Act and Y.K.K. Zipper Co. of Canada* (1975), [1975] F.C. 68 at 75, the Federal Court of Appeal held that, where a question of fact is determined by a statutorily created body having the legal authority and expertise necessary to evaluate the evidence and make such a finding, it would be improper to disturb the finding unless the court is satisfied that there is no evidence upon which the finding could have been made or that a wrong principle was applied in making it.

A court will be reluctant to interfere with a finding of fact unless there is complete evidence before it that the tribunal, being specialized and having the background knowledge not available to the courts, could not reasonably have made such a finding (*McCulloch of Canada Ltd.* v. *Antidumping Tribunal* (1977), [1978] 1 F.C. 222 (A.D.); *Rohm & Haas Canada Ltd.* v. *Antidumping Tribunal, supra; Remington Arms of Canada* v. *Les Industries Valcartier* (1981), [1982] 1 F.C. 586 (A.D.); *Hetex Garn A.G.* v. *Antidumping Tribunal* (1977), [1978] 2 F.C. 507 (A.D.); *Sarco Canada Ltd.* v. *Antidumping Tribunal, supra; PPG Industries Ltd.* v. *Antidumping Tribunal, supra*).

In *Rohm & Haas Canada Ltd.* v. *Antidumping Tribunal, supra,* the Federal Court of Appeal established the criteria necessary for review under section 28(1)(c) of the *Federal Court Act*:

- The tribunal must have made an erroneous finding of fact.
- That finding must have been made: (1) in a perverse or capricious manner, or (2) without regard for the material before it.

Findings that are in minor ways at variance with the evidence to which the tribunal has properly referred, cannot be said to be made "without regard for the evidence." Perversity implies willfully going contrary to the evidence, and the words "without regard for the material before it" connote that the tribunal must have ignored or refused to take notice of the material or some significant part of it. The court's conclusion that the decision attacked was based on an erroneous finding must be based on a reading of the tribunal's reasons as a whole (*Hetex Garn A.G.* v. *Antidumping Tribunal, supra; McCulloch of Canada Ltd.* v. *Antidumping Tribunal, supra*).

It would appear that a challenge under section 28(1)(c) could be based on additional evidence led, with the court's leave, on questions of fact as well as on evidence on the record made before the tribunal (*Rohm & Haas Canada Ltd.* v. *Antidumping Tribunal, supra*).

Establishment of Binational Panels

Introduction

The binational panels are to be established in accordance with the provisions of Annex 1901.2 which deal with matters such as: the creation of a roster of individuals to serve as panelists, the appointment of panelists to a binational panel, voting, a code of conduct governing panelists and undertakings as to confidentiality.

Roster of Panelists

Prior to January 1, 1989, Canada and the United States must develop a roster of 50 individuals to serve as panelists--each party selecting 25 candidates. All candidates must be citizens of Canada or the United States, be of good character, high standing and repute, and shall be chosen strictly on the basis of objectivity, reliability, sound judgment and general familiarity with international trade law. No candidate can be affiliated with either party; judges are not considered to be so affiliated (Annex 1901.2(1)).

Composition of Panels

A majority of the panelists on each panel shall be lawyers in good standing (Annex 1901.2(2)). Within 30 days of a request for a panel, each party shall appoint two panelists which should normally be from the roster of panelists. If a panelist is not selected from the roster, the panelist must be chosen in accordance with the criteria set out in Annex 1901.2(1). Each party has the right to exercise four peremptory challenges to be exercised simultaneously and in confidence, disqualifying from appointment to the panel up to four candidates proposed by the other party. These peremptory challenges and the selection of alternative panelists must occur within 45 days of the request for the panel. If a party fails to appoint its members to a panel within 30 days or, if a panelist is struck and no alternative panelist is selected within 45 days, such panelist shall be selected by lot on the 31st or 46th day, as the case may be, from that party's candidates on the roster (Annex 1901.2(2)).

Within 55 days of the request for a panel, the parties shall agree on the selection of a fifth panelist. If they are unable to agree, the four appointed panelists shall select the fifth panelist from the roster, by agreement, within 60 days of the request for a panel. If there is no agreement among the four appointed panelists, on the 61st day the fifth panelist shall be selected from the roster by lot, excluding candidates eliminated by peremptory challenges (Annex 1901.2 (3)).

With the appointment of the fifth panelist, the panelists shall promptly appoint a chairman from among the lawyers on the panel by a majority vote of the panelists. If there is no majority vote, the chairman shall be appointed by lot from among the lawyers on the panel (Annex 1901.2(4)).

Decisions of the panel shall be by a majority vote of all members of the panel. The panel shall issue a written decision with reasons, together with any dissenting or concurring opinions of the panelists (Annex 1901.2(5)).

If a panelist becomes unable to fulfill panel duties or is disqualified, proceedings of the panel shall be suspended pending the selection of a substitute panelist in accordance with the above procedures (Annex 1901.2(9)).

Confidentiality

Each panelist is required to sign a protective order for information supplied by the United States or its persons, covering business, proprietary and other privileged information and an undertaking for information supplied by Canada or its persons, covering confidential, personal, business, proprietary and other privileged information

(Annex 1901.2(7)). Canada and the United States have agreed to establish appropriate sanctions for violations of undertakings and protective orders. Each party has agreed to enforce sanctions with respect to any person within its jurisdiction. Failure by a panelist to sign a protective order or undertaking shall result in his or her disqualification (Annex 1901.2(8)).

Code of Conduct

The parties have agreed that, by the date of entry into force of the Agreement, they will exchange letters establishing a code of conduct for panelists (Article 1910). Panelists are subject to the code of conduct established pursuant to Article 1910. If a party believes that a panelist is in violation of the code, the parties shall consult and if they agree, the panelist will be removed and a new panelist selected (Annex 1901.2(6)).

Subject to the code of conduct, a panelist may engage in other business during the term of the panel, provided that this does not interfere with a panelist's performance of his or her duties (Annex 1901.2(10)).

While acting as a panelist, a panelist may not appear as counsel before another panel (Annex 1901.2(11)).

With the exception of violations of protective orders or undertakings signed by panelists, panelists shall be immune from suit and legal process relating to acts performed by them in their official capacity as panelists (Annex 1901.2(12)).

Remuneration

The remuneration of panelists, their travel and lodging expenses, and all general expenses of the panel shall be borne equally by the parties (Annex 1901.2(13)).

Establishment of the Secretariat

The parties have agreed to establish permanent Secretariat offices to facilitate the operation of the binational panel dispute settlement mechanism in antidumping and countervailing duty cases (Article 1901(1)).

The permanent offices of the Secretariat shall be in Washington and Ottawa. Each party shall be responsible for the operating costs of its Secretariat office. Canada shall appoint the secretary of the Canadian section of the Secretariat and the United States shall appoint the secretary of the U.S. section. The secretaries will be responsible for all administrative matters involving their respective offices. They shall act jointly to service all meetings of panels (Article 1909(8)). The secretary of the country in which a panel proceeding is held shall prepare a record thereof and each secretary shall preserve an authentic copy of the same in the permanent offices (Article 1909(8)).

Each secretary shall receive and file all requests, briefs and other papers properly presented to a panel or committee in any proceeding before it (Article 1909(9)).

The secretaries shall forward to each other copies of all official letters, documents, records or other papers received or filed with the Secretariat office which pertain to any proceeding before a panel or committee, so that there shall be on file in each office of the Secretariat either the original or a copy of all official letters and other papers relating to all proceedings (Article 1909(10).

Panel Procedures

Requests For Review

Either party may request that a panel review, based upon the administrative record, a final AD or CVD determination of a competent investigating authority of either party to determine whether such determination was in accordance with the AD or CVD laws of the importing party. The Agreement has defined the terms "administrative record," "final determination," "competent investigating authority," "antidumping or countervailing duty law," "antidumping statute" and "countervailing duty statute." These definitions are set out in Appendix "A".

A final determination in the case of the Canadian Import Tribunal includes an affirmative or negative finding of injury and a decision to initiate a review. Public interest reports issued by the Canadian Import Tribunal, or advice by the tribunal given to the Deputy Minister as a result of a referral to the tribunal, are not reviewable by the binational panels. A final determination in the case of the Deputy Minister includes two decisions of the Deputy Minister that cannot at present be appealed under the provisions of the *Special Import Measures Act*: (1) final determinations of dumping or subsidizing, and (2) reviews of undertakings. In addition, the binational panels can review redeterminations made by the Deputy Minister which can presently be appealed to the Tariff Board.

Persons who would otherwise be entitled to commence domestic procedures for judicial review can initiate a panel review (Article 1904(5)). These persons include domestic producers, importers and exporters who were involved in the proceedings before the Canadian

Import Tribunal, the U.S. International Trade Commission, the Canadian Department of National Revenue and the U.S. Department of Commerce.

The Free Trade Agreement does not eliminate judicial review by domestic courts in cases where a binational panel is not requested by Canada or the United States. A written request for a panel shall be made within 30 days following the date of publication or notice of the final determination. Failure to request a binational panel review within the specified time precludes a review by the panel (Article 1904(4)).

Rules of Procedure

The panels shall conduct their review in accordance with the procedures established by the parties pursuant to Article 1904(14). The parties have agreed to adopt rules of procedure by January 1, 1989. Such rules shall be based, where appropriate, on judicial rules of appellate procedure and shall include rules concerning: the content and service of requests for panels; a requirement that the competent investigating authority transmit to the panel the administrative record of the proceedings; the protection of business, proprietary and other privileged information (including sanctions against persons participating before panels for improper release of such information); participation by private persons; limits on panel review to errors alleged by the parties or private persons; filing and service; computation and extensions of time; the form and content of briefs and other papers; "pre" and "post" hearing conferences; oral arguments; requests for rehearing; and voluntary terminations of panel review (Article 1904(14)).

The rules shall be designed to result in final decisions within 315 days of the date on which a request for a panel is made, and shall allow:

- 30 days for filing of the complaint
- 30 days for designation or certification of the administrative record and its filing with the panel
- 60 days for the complainant to file its brief
- 60 days for the respondent to file its brief
- 15 days for filing of reply briefs
- 15 to 30 days for the panel to convene and hear oral arguments
- 90 days for the panel to issue its written decision (Article 1904(14)).

The competent investigating authority who issued the final determination in question shall have the right to appear and be represented by counsel before the panel. In addition, persons who, pursuant to the law of the importing party, would otherwise have standing to appear and be represented in a domestic judicial review proceeding concerning the determination of the competent investigating authority, shall have the right to appear and be represented by counsel before the panel (Article 1904(7)).

Decisions of Binational Panels

Remands

The panel may uphold a final determination or remand it for action not inconsistent with the panel's decision. Remand has been defined as "referral back for a determination not inconsistent with the panel or committee decision" (Article 1911). Where the panel remands a final determination, the panel shall establish as brief a time as is reasonable for compliance with the remand, taking into account the complexity of the facts and legal issues involved and the nature of the panel's decision. In no event shall the time permitted for compliance with the remand exceed the maximum (counted from the date of the filing of the petition, complaint or application) permitted by statute for the competent investigating authority in question to make a final determination of an investigation. If review of the action taken by the competent investigating authority is needed, such review shall be made before the same panel, which shall issue a final decision within 90 days of the date on which such remand action is submitted (Article 1904(8)).

Extraordinary Challenge Procedure

The Agreement provides for an extraordinary challenge procedure set out in Annex 1904.13 which can be invoked within a reasonable time after a panel decision is issued and a party alleges that:

1.
    - a member of the panel was guilty of gross misconduct, bias or a serious conflict of interest, or otherwise materially violated the rules of conduct.
    - the panel seriously departed from a fundamental rule of procedure.
    - the panel manifestly exceeded its powers, authority or jurisdiction set forth in this article.

2. if any of the actions set out in (1) above have materially affected the panel's decision and threatens the integrity of the binational panel review process (Article 1904(13)).

Annex 1904.13 provides that the parties shall establish an extraordinary challenge committee, comprised of three members, within 15 days of a request. The members shall be selected from a ten-person roster comprised of judges or former judges of a U.S. federal court or a Canadian court of superior jurisdiction. Each party shall name five persons to this roster. Each party shall select one member from this roster and the third shall be selected from the roster by the two members chosen by the parties or, if necessary, by lot from the roster.

The parties have agreed to establish rules of procedure for an extraordinary challenge committee by January 1, 1989. The rules shall provide for a committee decision typically within 30 days of its establishment (Annex 1904.13(2)).

Committee decisions shall be binding on the parties. If the grounds for invoking the extraordinary challenge procedures have been established, the committee shall vacate the original panel decision or remand it to the original panel for action not inconsistent with the committee's decision. If the grounds are not established, the committee shall affirm the original panel decision. If the original decision is vacated, a new panel shall be established pursuant to Annex 1901.2 (Annex 1904.13(3)). It is expected that the extraordinary challenge procedure will be invoked sparingly. This may not be so, however, if a broad interpretation is given to the allegation that a panel manifestly exceeded its powers, authority or jurisdiction.

Jurisdiction of Domestic Courts To Review Decisions of Binational Panels

Decisions of the binational panels will be binding on Canada and the United States (Article 1904(9)). The parties have agreed that a final determination shall not be reviewed if either party requests a panel. In addition, neither party shall, in its domestic legislation, provide for an appeal from a panel decision to its domestic courts (Article 1904(11)).

The question arises whether, notwithstanding this privative clause, a domestic producer, importer or exporter, dissatisfied with a panel decision, can seek to have the decision overturned by a superior court of one of the Canadian provinces. Can Parliament legislate the removal of jurisdiction to judicially review decisions of an inferior tribunal from either or both the Federal Court of Canada and the superior courts of the provinces? At present, judicial review of decisions of the Canadian Import Tribunal is sought in the Federal Court of Appeal pursuant to section 28 of the *Federal Court Act*, and decisions of the Deputy Minister of National Revenue for Customs and Excise can be appealed to the Tariff Board pursuant to the *Special Import Measures Act*. Parliament clearly has the authority to amend these acts so as to comply with the provisions of the Free Trade Agreement. In the light of sections 96 to 100 of the *Constitution Act, 1867*, however, can Parliament legislate so as to deny the superior courts their traditional authority to review decisions of inferior tribunals?

The extent to which Parliament and the provincial legislatures may act in a manner which derogates from the powers of the superior courts in Canada has been the subject of extensive debate. On one side, Professor William R. Lederman and others have consistently advocated that sections 96 to 100 of the *Constitution Act, 1867* create a guaranteed core of superior court jurisdiction upon which it is not permissible for Parliament or the provinces to encroach (see W.R. Lederman, *Continuing Canadian Constitutional Dilemmas* (Toronto: Butterworths, 1981) at 109 and 175). The opposite view, including the views of Professor Peter Hogg, maintain that the *Constitution Act, 1867* does not establish a constitutional separation of powers whereby the legislature, the executive and the judiciary have guaranteed cores of jurisdiction (see P.W. Hogg, *Constitutional Law of Canada*, 2d ed. (Toronto: Carswell, 1985) at 164).

In the eyes of a number of commentators, recent decisions of the Supreme Court of Canada have supported Professor Lederman's position (see D.J. Mullan, "Developments in Administrative Law: The 1982-83 Term" (1984) 6 Sup. Ct L. Rev. 1 at 5-7; J.D. Whyte, "Developments in Constitutional Law: The 1982-83 Term" (1984) 6 Sup. Ct L. Rev. 49 at 74-81). If this view is adopted, it might be argued that Parliament cannot legislate so as to deprive the superior courts of their inherent jurisdiction to review the decisions of a binational panel.

Conclusion

The Canadian government has claimed that judicial review of final antidumping and countervailing duty determinations by binational panels will guarantee the impartial application of Canadian and American laws, and will create predictability and security of access for Canadian exporters of goods to the U.S. market.

The function of the binational panels is to review decisions of the Department of National Revenue, the Canadian Import Tribunal, the Department of Commerce and the International Trade Commission based on the same standard of review that is presently applied by Canadian and American appellate courts. What evidence suggests that Canadian and American appellate courts have not impartially applied Canadian and U.S. AD and CVD laws of judicial review? In Canada, there is no evidence that the Federal Court of Appeal and the Tariff Board have rendered partial decisions.

One must also question why nonlawyers will be making purely legal decisions of judicial review. Will this affect the quality of judicial review rendered by the panels? The concept of appointing lay persons to administrative tribunals has great merit when lay persons are making decisions of fact (i.e., the Competition Tribunal), but not decisions of law. In addition, because the panels are *ad hoc* and selected from a roster of 50 candidates, there will not necessarily be any continuity of membership on the panels. How closely one panel will follow a decision of another will affect this continuity.

The creation of binational panels is indeed unique. It remains to be seen, however, whether Canadian producers, importers and exporters will be better served by the binational panels. One can only hope that judicial review of final AD and CVD determinations does not become politicized, and that the panelists will be loyal to the effective functioning of the Agreement rather than to the country that appointed them.

Appendix A

Administrative record, unless otherwise agreed by the parties and the other persons appearing before a panel, means:

- all documentary or other information presented to or obtained by the competent investigating authority in the course of the administrative proceeding, including any governmental memoranda pertaining to the case, and including any record of *ex parte* meetings as may be required to be kept
- a copy of the final determination of the competent investigating authority, including reasons for the determination
- all transcripts or records of conferences or hearings before the competent investigating authority
- all notices published in the *Canada Gazette* or the *Federal Register* in connection with the administrative proceeding (Article 1911).

Final determination means:

1. In the case of Canada:

   (i) an order or finding of the Canadian Import Tribunal under subsection 43(1) of the *Special Import Measures Act*

   (ii) an order by the Canadian Import Tribunal under subsection 76(4) of the *Special Import Measures Act*, continuing an order or finding made under subsection 43(1) of the act with or without amendment

   (iii) a determination by the Deputy Minister of National Revenue for Customs and Excise pursuant to section 41 of the *Special Import Measures Act*

   (iv) a redetermination by the Deputy Minister pursuant to section 59 of the *Special Import Measures Act*

   (v) a decision by the Canadian Import Tribunal pursuant to subsection 76(3) of the *Special Import Measures Act* not to initiate a review

   (vi) a reconsideration by the Canadian Import Tribunal pursuant to subsection 91(3) of the *Special Import Measures Act*

   (vii) a review by the Deputy Minister of an undertaking pursuant to section 53(1) of the *Special Import Measures Act*.

2. In the case of the United States:
   - (i) a final affirmative determination by the International Trade Administration of the U.S. Department of Commerce or by the U.S. International Trade Commission under section 705 or 735 of the *Tariff Act* of 1930, as amended, including any negative part of such a determination
   - (ii) a final negative determination by the International Trade Administration of the U.S. Department of Commerce or by the U.S. International Trade Commission under section 705 or 735 of the *Tariff Act* of 1930, as amended, including any affirmative part of such a determination
   - (iii) a final determination, excluding a determination as in (iv) below, under section 751 of the *Tariff Act* of 1930, as amended
   - (iv) a determination by the U.S. International Trade Commission under section 751(b) of the *Tariff Act* of 1930, as amended, not to review a determination based upon changed circumstances
   - (v) a determination by the International Trade Administration of the U.S. Department of Commerce whether a particular type of merchandise is within the class or kind of merchandise described in an existing finding of dumping or antidumping or countervailing duty order (Articles 1911 and 1904(10)).

Competent investigating authority means:

1. In the case of Canada:
   - the Canadian Import Tribunal, or its successor
   - the Deputy Minister of National Revenue for Customs and Excise as defined in the *Special Import Measures Act*, or his successor.

2. In the case of the United States:
   - the International Trade Administration of the U.S. Department of Commerce, or its successor
   - the U.S. International Trade Commission, or its successor (Article 1911).

Antidumping or countervailing duty law consists of the relevant statutes, legislative history, regulations, administrative practice, and judicial precedents to the extent that a court of the importing party would rely on such materials in reviewing a final determination of the competent investigating authority (Article 1904(2)).

Antidumping statute, as referred to in Articles 1902 and 1903, means:

1. in the case of Canada, the relevant provisions of the *Special Import Measures Act*, as amended, and any successor statutes
2. in the case of the United States, the relevant provisions of Title VII of the *Tariff Act* of 1930, as amended, and any successor statutes
3. the provisions of any other statute that provides for judicial review of final determinations under items (1) or (2) above, or indicates the standard of review to be applied (Article 1911).

Countervailing duty statute, as referred to in Articles 1902 and 1903, means:

1. in the case of Canada, the relevant provisions of the *Special Import Measures Act*, as amended, and any successor statutes
2. in the case of the United States, section 303 and the relevant provisions of Title VII of the *Tariff Act* of 1930, as amended, and any successor statutes
3. the provisions of any other statute that provide for judicial review of final determinations under items (1) or (2) above, or indicate the standard of review to be applied (Article 1911).

Notes

1. This section of the paper has been authored by Kate Murray. It has been extracted from the manuscript of *The Canadian Trade Law Reporter* (John D. Richard & Richard G. Dearden) to be published by CCH Canada Limited in 1988.

Improvements in Trade Remedy Law and Procedures under the Canada-United States Free Trade Agreement

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On January 2, 1988, President Ronald Reagan and Prime Minister Brian Mulroney signed the Canada-United States Free Trade Agreement (FTA). The Agreement is intended to establish fair and predictable conditions to further the ability of Canadians and Americans to do business in each other's country.

The most significant changes that the FTA makes to trade remedy laws are procedural: provisions for a binational dispute-resolution system to resolve trade-related disputes between the two countries. The FTA provides binding decisions for all "escape clause" disputes, all binational reviews of final antidumping (AD) or countervailing duty (CVD) decisions and any other matters affecting the operation of the Agreement that the two parties agree to refer to binding arbitration. The dispute-resolution system will also shorten the time for resolving these disputes. This should ameliorate the chilling effect on trade that such disputes can create as they slowly wind through the courts or the dispute-resolution mechanisms of the General Agreement on Tariffs and Trade (GATT). The involvement of citizens from both countries in the dispute-resolution process should, in turn, promote harmonization of the trade remedy laws of the two countries. This is beneficial insofar as the FTA provides that the two governments will negotiate common rules in the AD/CVD area to replace the current ones, increasingly perceived as outmoded or barriers to economically desirable trade.

Elements of the Dispute-Resolution Mechanisms

The FTA provides two separate mechanisms for resolving trade disputes between the United States and Canada. Chapter 18 of the FTA (Institutional Provisions) establishes the general procedures for resolving disputes under the Agreement, with the exception of disputes relating to the provision of financial services and AD/CVD cases (Article 1801.1). Chapter 19 of the Agreement establishes a specific binational panel dispute-resolution mechanism to review final AD and CVD determinations as well as proposed amendments to either country's AD or CVD statutes (Articles 1901, 1903 and 1904).

General Procedures

Under the general dispute-resolution procedures, each country must provide written notice to the other country of "any proposed or actual measure" that might materially affect the operation of the Agreement (Article 1803.1). Each country is required to promptly respond to questions or requests for information from the other country (Article 1803.3). There are provisions for either country to request consultations regarding "any actual or proposed measure or any other matter" that it considers affects the operation of the FTA (Article 1804.1). The right of consultation exists regardless of whether or not a matter was previously notified. Hence, neither country can easily avoid their obligation to discuss proposed or actual measures affecting the operation of the Agreement.

If the parties fail to resolve a matter through consultations within 30 days, either country may refer the matter to the Canada-United States Trade Commission established under the Agreement (Article 1802.1). The commission supervises the proper implementation of the Agreement, resolves disputes concerning its interpretation and application, oversees its further elaboration and considers any other matter that affects its operation. The commission will comprise of representatives from both countries, the principal representatives being the cabinet-level officer or minister primarily responsibile for U.S. or Canadian international trade, or his or her designee. (Article 1802.2).

If the commission fails to resolve a dispute within 30 days, it may refer the dispute to a binding arbitration panel, with the interesting exception that disputes involving escape clause actions must be sent to a binding arbitration panel (Article 1806.1(a)). Should the commission not refer a dispute to binding arbitration, either country may request that the commission establish a panel of experts to consider the matter (Article 1807.2). If the commission is so requested, it must establish such a panel to inquire into the dispute.

Binding Arbitration

With respect to matters referred to binding arbitration, the commission may adopt the terms within which the arbitration panels are to operate (Article 1806.1). Unless the commission specifically directs otherwise, the panels are to consist of five members—at least two Canadian citizens and two Americans—selected from a roster established by the commisison. Selection of the panelists is completed within strict time frames. If a country fails to appoint its two panelists within 15 days or if the four appointed panelists fail to decide on the fifth within 30 days, the panelists are selected by lot from the roster (Article 1807.3).

The panel's findings are final and binding on both governments; no further report back to or action by the commission is contemplated. If a country fails to comply with the panel findings in timely fashion, and if the two countries are unable to agree on the appropriate compensation or remedial action, the other country may retaliate by suspending application of equivalent benefits under the FTA to the offending country (Article 1806.3).

Nonbinding Expert Panels

Should the commission fail to either resolve a matter after 30 days or refer it to binding arbitration, it will, upon the request of either country, establish a panel of experts to investigate the matter. Within three months, the expert panel will present the two countries with an initial report containing: its findings of fact; its determination whether the matter under consideration is inconsistent with the FTA, or whether it would nullify or impair any rights or benefits under it; and recommendations, if any, for the resolution of the dispute. Both countries will have an opportunity to present reasons for their disagreement with the report. The panel may make further examinations if it deems appropriate and it must issue a final report within 30 days of issuing the initial report (Articles 1807.5 and 1807.6).

After receiving the final report, the commission must agree to resolve the dispute. Normally, the commission's decision should accord with the panel's recommendation. Whenever possible, the resolution should be the non-implementation or removal of any measure that does not conform to the FTA or that nullifies or impairs rights or benefits under it or, failing such a resolution, compensation (Article 1807.8). This process focuses the remedy on the problem at hand, and it may prevent specific trade disputes from spilling into other areas. Because the decisions of the commission are by consensus, however, both parties must agree on any resolution. If the commission cannot reach a mutually satisfactory resolution within 30 days of receipt of the final panel report, the country that believes that its rights or benefits under the FTA would be impaired by the measure complained of may suspend application of equivalent benefits to the other country (Article 1807.9).

AD and CVD Binational Panel Dispute Settlement

The binational panels for settling disputes involving AD and CVD issues will operate entirely separate from the general dispute settlement mechanism, with a different roster of panelists and unique procedures. Either country may request review in two instances. First, either country may request that a binational panel issue a declaratory opinion whether a proposed amendment to the other country's AD or CVD statutes conforms to the GATT, the GATT Antidumping Code, the GATT Subsidies Code,[1] or the object and purpose of the FTA. The procedures for such review are discussed in greater detail later. Second, either country may request a binational panel to review a final agency order in an AD or CVD case.

Replacement of domestic judicial review of final AD/CVD orders in the United States or Canada will occur whenever a country requests such review, either on its own initiative or at the request of a person who would otherwise be entitled to commence domestic procedures for judicial review of such a final determination (Article 1904.5). Persons who would otherwise have standing to appear in domestic judicial review proceedings shall have the right to appear, as will the competent investigating authority who issued the final determination in question (Article 1904.7).

The binational panel is required to apply the law and standard of judicial review applicable in the investigating country to determine whether the agency decision in question complies with the AD or CVD law of that country (Articles 1904.2 and 1904.3). That is, each country is judged in terms of whether it lives up to its own rules, not to a set of binational or supranational standards. In the United States, the reviewing court (and thus the panel) is to hold an agency determination unlawful if it is "arbitrary, capricious, [or] an abuse of discretion"; "unsupported by substantial evidence on the record"; or "otherwise not in accordance with the law" (19 U.S.C. § 1516a(b)(1)). In Canada, the reviewing court may reverse a final agency order for failing to observe a principle of natural justice or for otherwise acting beyond or refusing to exercise its jurisdiction, for erring in law in making its decision, or for basing its decision on an erroneous finding of fact made in a perverse or capricious manner or without regard for the material before the agency.[2]

A panel may either uphold the agency decision or remand the decision to the relevant agency with specific instructions (Article 1904.8). Panel decisions are binding on the relevant agencies in the United States and Canada (Article 1904.9). Strict timetables govern the procedures for filing complaints and hearing disputes; the binational panel must issue its decision within 300 to 315 days of the request for a panel (Article 1904.14). Similarly, upon remand of a final determination, the panel must determine as brief a time as is reasonable for compliance with the remand (which in no event shall exceed the time permitted for the investigating authority in question to make a final determination (Article 1904.8)).

In extraordinary circumstances, if either country believes the integrity of the binational panel review process to be threatened (by gross misconduct, bias or serious conflict of interest of a panel member; by a departure from a fundamental rule or procedure; or by a panel manifestly exceeding its jurisdiction), it can request an extraordinary challenge committee to review the binational panel's decision (Article 1904.13). This committee consists of three members chosen from a ten-person roster comprised of former or current U.S. federal court judges or Canadian superior court judges. The challenge committee is the court of last resort in the binational panel review process. It must render its decision within 30 days, which decision is binding on both member countries (Article 1904.13).

The binational review mechanism for dispute settlement in AD/CVD cases will be in effect for five years. During this period, the two countries are to cooperate to develop a "substitute system" of AD/CVD laws applicable to both countries. An extension of two years to the binational review mechanism is possible. Failure to reach agreement on a common system of AD/CVD laws within seven years, however, enables either party to terminate the Agreement on six month's notice (Article 1906).

The Binding Dispute-Resolution Mechanisms for AD/CVD Cases Improve Existing Judicial Review Procedures

At present, Canadians who are dissatisfied with final determinations made by the U.S. Department of Commerce (Commerce) or the International Trade Commission (ITC) in an AD or CVD investigation may appeal that determination to the Court of International Trade (CIT), with a further right of appeal to the Court of Appeals for the Federal Circuit (CAFC) if necessary.[3] There are no statutory deadlines for final decisions from these courts. An appeal from a

Commerce or ITC decision to the CIT takes at least a year; a delay of two to three years between the agency determination and the final CIT decision is not unusual. Consequently, parties intending to appeal such decisions customarily allocate at least a two-year period for the appeal.[4] A subsequent appeal to the CAFC could add another year or more to the appellate process. This creates a very practical problem for litigants, who must continue to deposit the estimated amount of the duty for the full period. Counsel often advise their clients that an appeal is simply not worth the time and money involved.

In Canada, the Department of National Revenue, Customs and Excise (DNR) and the Canadian Import Tribunal (Tribunal) make determinations on whether dumping or subsidies exist and whether these cause or are likely to cause material injury to Canadian products. Parties may seek judicial review of a final order of the Tribunal in the Federal Court of Appeal (FCA).[5] Certain DNR determinations may be appealed to the Tariff Board and then to the FCA on questions of law. In rare instances, appeals from the FCA may be heard by the Supreme Court of Canada. This appeal process can range from two to four years.

For several reasons, the AD/CVD dispute settlement mechanisms under the FTA represent a substantial improvement over existing methods of judicial review and will be of great practical significance to U.S. and Canadian petitioners and respondents involved in AD or CVD cases.

Efficiency

The most striking improvement is that the binational panel review process will operate faster than the current U.S. and Canadian judicial review procedures. As noted above, the FTA dispute-resolution mechanisms for AD/CVD cases would be subject to a deadline of 300 to 315 days, measured from the end of the administrative proceeding under review.[6] Thus, final review of AD/CVD determinations will occur in less time than it usually takes to obtain a decision from the U.S. CIT or Canadian FCA alone (which do not exhaust the existing appellate review process). This maximum time limit will eliminate the opportunity for open-ended delays under current U.S. and Canadian law[7] and it will provide the parties with an improved ability to calculate the economic costs and benefits of an appeal.

Uniformity

A second practical advantage of the binational dispute-resolution mechanism is the likelihood of increased consistency in decision making that will result from multimember panels. In contrast to group decision making, the nine judges on the U.S. CIT (as well as six judges of senior status) sit, hear cases and issue decisions individually.[8] Interpretations of the law can vary significantly from judge to judge even though each formally applies the same laws and standard of review.[9] While the CAFC ensures eventual uniformity, the current system is less than ideal. The CAFC eliminates differences in legal reasoning and conclusions among the CIT judges only after they occur, and the additional appeal increases delay and uncertainty.[10]

The multimember nature of the AD/CVD review panels will eliminate the possibility of individual, idiosyncratic interpretations of either country's AD/CVD laws and should prevent the adoption of extreme positions. To achieve panel consensus, moderate decisions, by definition, will be necessary. This, in turn, should facilitate consistency among panel decisions over time. While the membership of the panels will vary from case to case, the likelihood of recourse to previous panel decisions in future cases will help to ensure continuity and consistency in panel decisions.

Balance and Equity

An additional improvement over the existing judicial review systems is that the FTA procedures (and in particular the binational composition of the AD/CVD review panels) should ensure a well-balanced voicing and recognition of Canadian and U.S. interpretations of AD/CVD laws. U.S. and Canadian appointees will each make up at least two of the five members of the panel. In addition, the private parties involved in AD/CVD cases, the investigating agency whose decision is under review, as well as both countries each have the right to present arguments before the panel. Because representatives from the United States and Canada will take part in the actual decision making under the FTA, the views of all parties are likely to receive full and fair consideration.

Currently, each country may express its views on the application of the other's AD/CVD laws in specific cases if that country is a party to the proceedings. But neither country can actively participate in the review of investigations of its neighbour. Thus, the binational character of the panels should promote a more equitable application, or at least the perception of equitable application, of each country's AD/CVD laws to industries in the other country. As the two countries work together to interpret each other's law and as the respective agencies work to administer the jointly interpreted law, there should be a convergence in the application of the already quite similar trade remedy laws of both countries.

Improved Climate

The binational nature of the dispute-resolution system will also increase the perception among businessmen of fair and impartial application of AD/CVD laws. Regardless of whether current AD and CVD decisions are in fact influenced by political factors, the *perception* that such cases are decided on political grounds can affect business behaviour. Confidence in the fair application of each country's trade laws should improve business climate and increase the willingness to export to the other country. This, in turn, should help eliminate any distortion of investment between the two countries and should exploit more efficiently the comparative advantages.

Improved Access and Representation

The AD/CVD dispute-resolution system also provides small businesses with enhanced representation. At present, businesses and trade associations must themselves appeal to the U.S. CIT, CAFC and the Canadian FCA (sovereign governments rarely appear in the domestic courts of a foreign government). These appeals represent a considerable financial burden. Under the FTA, a private party entitled to seek review of a final agency determination in the domestic courts may request that its government initiate review by a binational panel. If so asked, the government *must* comply. As a result, a small business or trade association, which could not afford to challenge an agency ruling under the current system, can now have its government present its point of view to a binational review panel (although there is no guarantee that either government, which has its own agenda and priorities, will press private party claims as vigorously as the parties might wish).

Not surprisingly, commentators have criticized the FTA's binational review mechanism for failing to address alleged defects in the content or application of U.S. and Canadian AD/CVD laws. Some, for example, have criticized the binational review procedure because it continues to apply the standard of judicial review currently employed under U.S. and Canadian law, the implication being that this standard is not sufficiently rigorous. But the standard of review of the U.S. CIT parallels that set forth in the *Administrative Procedure Act* (see 5 U.S.C. § 706), and it is typical of the level of scrutiny that U.S. courts employ in reviewing decisions of agencies that are vested with specialized expertise. This standard should provide an appropriate level of scrutiny. Indeed, under the current U.S. system, the CIT has reversed, remanded or modified final agency determinations in numerous instances.[11]

The criticism that the Canadian standard of review is not sufficiently rigorous carries more weight.[12] The FCA has remanded only 4 of 17 cases to the Tribunal since 1979.[13] It has not remanded a case since 1983. It remains to be seen whether the AD/CVD binational review panels will add teeth to the Canadian standard of review, perhaps by interpreting the standard to conform more closely to that of the United States.

Additionally, some Canadians complain that the critical problem for Canadian exporters is not adverse final determinations of Commerce or the ITC, but rather adverse preliminary determinations, which would remain outside the scope of the binational review mechanism. There are several points worth noting here. To begin, preliminary determinations are not inevitably adverse ones (that is, the ITC does not automatically make an affirmative preliminary finding of injury). Although the threshold for finding injury at the initial stage is quite low, the ITC terminated 58 AD investigations at the preliminary stage between 1980 and 1986 (that is, made a negative finding), five of which involved Canadian products.[14]

More important, the U.S. judicial system does not look favourably upon interlocutory appeals; interim appeals disrupt the review process, can unduly delay proceedings and may involve appellate judges before all the facts are known. Consistent with this view, affirmative preliminary findings do not become "cast in stone." In a number of cases after a preliminary determination of injury, the ITC has ruled at the final stage that the imports at issue were not causing injury to the domestic industry.[15] Likewise, Commerce has substantially modified a preliminary affirmative determination of dumping or subsidization in its final determination in a number of cases.[16] If a final determination repeats the mistakes of an erroneous preliminary determination, however, the binational review mechanism of the FTA will provide a faster, less costly and more impartial method of review and redress.

Perhaps most important in practical terms, there is no evidence to support the claim that exports are seriously affected by the imposition of provisional AD or CVD duties in cases where the exporters are successful at the final determination stage. In both the United States and Canada, any provisional duties collected are promptly refunded. Furthermore, the FTA will not alter the administrative and judicial procedures that provide recourse for return of such duties.

The Dispute-Resolution Mechanisms Provide Unparalleled Protection Against Changes in Trade Remedy Laws

The FTA's dispute-resolution mechanisms apply not only to specific cases, but to proposed changes in either country's legislation which the other country believes might materially affect the operation of the

FTA. Chapter 19 of the FTA prohibits the United States and Canada from applying changes in its AD/CVD laws to the other country unless: the amending legislation specifically states that it will apply to the other country (something which Congress and Parliament have sought to avoid in the past); there is prior notification and, if requested, consultations with the other country; and the changes are consistent with the GATT Antidumping and Subsidies codes as well as with the object and purpose of the FTA.[17]

If a dispute is not resolved by consultations, either country may refer the matter to a binational panel (Article 1903). These five-member panels are chosen from the same roster and are established in the same fashion as those that review final AD/CVD decisions. The panel issues a declaratory opinion whether the proposed amendment is consistent with the GATT Antidumping and Subsidies codes and with the object and purpose of the FTA, or whether the amendment would, in effect, overturn a prior decision of the binational dispute settlement panel (Article 1903.1).[18] If the panel recommends modifications to the proposed AD/CVD law, the two countries must consult to achieve a mutually satisfactory solution within 90 days of the panel's opinion. After the 90-day period, if no mutual resolution is reached or if no remedial legislation is enacted within nine months, the complainant government may take comparable legislative or executive action or terminate the FTA with sixty day's notice (Article 1903.3).

As described above, the general dispute-resolution mechanisms similarly require each country to provide written notice to the other of any "proposed or actual measure"—which includes proposed changes in legislation, regulations, or government practice (other than AD/CVD legislation)—that might materially affect the operation of the FTA. Also, either country may request consultations regarding any actual or proposed measure, whether or not notified, that it believes might materially affect the operation of the FTA (Articles 1803.1 and 1804.1). This formal channel for communication represents a significant improvement over existing practice. Currently, the U.S. and Canadian governments are not notified of changes in the other's legislation, regulations or government practices affecting trade, much less do they have the right to request consultations with the other government concerning those changes.[19]

If consultations fail, the matter proceeds, in conformity with the general dispute-resolution provisions, to the commission and potentially to arbitration. As described above, if either government fails to implement the decisions of an arbitration panel within a reasonable time, it must provide compensation. If the two governments cannot agree on appropriate compensation, then the injured government may suspend the application of equivalent benefits under the FTA to the noncomplying government (Article 1806.3).

These remedies – the right of compensation and the sanction of withdrawal of equivalent benefits under the general dispute-resolution mechanism, or the sanction of equivalent counteraction under the AD/CVD system – make the dispute settlement mechanisms binding in international law. These are as binding a system as either country was ever likely to agree to.[20] Moreover, the sanctions, which are more effective than those in the vast majority of international agreements, offer a protection against changes in the other government's legislation and practices affecting trade that is superior to that generally found.[21] But because neither country is ultimately required to change its legislation, there is no significnt diminution of sovereignty of either country, its agencies or courts. Notwithstanding public rhetoric and resistance to binding dispute mechanisms, this is what the United States has been seeking in the GATT for 15 years, and should provide an important model for the Uruguay Round.

The Dispute Settlement Mechanisms of the FTA will Enhance the Development of a Common Body of Canadian-U.S. Trade Law

An added benefit of the FTA dispute settlement mechanisms is that they should contribute to the development of a common Canadian-U.S. system of trade laws. At a minimum, the AD/CVD and general dispute-resolution panels will ensure that legislative developments in each country remain consistent with the object and purpose of the FTA as well as the principles of the GATT. Furthermore, the binational nature of the dispute-resolution mechanisms should promote increased uniformity in the development and application of Canadian and U.S. trade law while a common system of trade law develops. The creation of a body of experts (panel members) familiar with the application of the other country's trade laws will aid the development and negotiation of common principles of trade law.[22]

The antidumping laws of the two countries are already quite similar and in the CVD area, each country's methodologies are reasonably similar. While admittedly the binational AD/CVD panels will be reviewing the results of AD and CVD investigations under existing Canadian or U.S. law, over time the panels should develop common approaches to specific areas of these laws. Common principles and approaches could, in turn, provide the foundation for future efforts to harmonize the conflicting areas of Canadian and U.S. trade law that remain. The five-year limitation on the dispute-resolution mechanisms (with the possibility of an extension of two years) will give the parties the time they need to understand the strengths, weaknesses and differences in each other's trade remedy laws and to develop the necessary shared approach. Moreover, the deadline should force concrete action.[23]

Changes in Application of the Escape Clause Significantly Improve Existing Substantive Law

The FTA significantly improves substantive trade remedy law, involving the application and review of action that either country takes under its respective escape clause provisions in accordance with GATT Article XIX. Whenever a country takes action under an escape clause, it proceeds against imports from all countries. In the United States, section 201 of the *Trade Act* of 1974 authorizes the President to take measures, including the imposition of duties and quantitative restrictions, against imports of a product from all countries if increased (albeit fairly traded) imports of that product are a substantial cause of serious injury or threat thereof to a domestic industry.[24] Canada has similar measures available under section 8 of the *Customs Tariff Act*[25] and section 5 of the *Export and Import Permits Act*.[26] Consequently, if the United States or Canada initiate successful actions, U.S. or Canadian products will inevitably be affected, even if products imported from third countries are largely responsible for the increase in imports and injury to the petitioning industry.[27]

In contrast, the FTA provides that if either country were to initiate an escape clause action, imports from the other country would be excluded from such a proceeding unless they were "substantial" and "contributing importantly" to the "serious injury or threat thereof caused by imports." Imports from the United States or Canada in the range of 5 to 10 per cent or less of the other country's total imports of the goods in question "would normally not be considered substantial."[28] Further, even if the other country's imports exceed the 5 to 10 per cent range, the FTA requires that they be excluded unless they are found to be "contributing significantly" to the injury.[29] The underlying decision to alter the substantive law in the escape clause area alone can perhaps best be explained by the still recognized distinction between fairly traded goods (which are affected by escape clause actions) and unfairly traded goods (which are addressed by AD/CVD and other measures). Because the United States is a large importer from many countries, and often no one country's goods are a large percentage of a particular imported product, these provisions may prove to be particularly advantageous for Canada.

Moreover, whenever a U.S. or Canadian escape clause action involves a product from the other country, the FTA will require the initiating government to notify the other government (and, if so requested, to enter into consultations) *prior* to taking action. Notably, the United States did not do this in the 1986 case on *Shakes and Shingles*.[30] Also, if the United States or Canada believes that an escape clause measure imposed by the other country is contrary to or impairs benefits anticipated under the FTA or the GATT, that country may request the commission to refer the matter to a binding arbitration panel, which the commission must do.

The Binational Dispute-Resolution Mechanisms Improve on GATT Procedures

International dispute resolution under the GATT panel procedures has not proven to be an entirely satisfactory mechanism to resolve trade disputes. GATT procedures emphasize conciliation of the parties, and panel decisions are not binding in their own right. Indeed, the consensus rule of the GATT allows the disputing parties to block adoption of panel reports (as the United States has done in several agricultural cases in the GATT Council).[31] The dispute-resolution mechanisms under the FTA will improve upon the GATT procedures in two significant fashions. First, the FTA dispute-resolution procedures for AD/CVD cases, escape clause actions and certain other matters are binding and the Agreement provides effective sanctions for failure to comply with panel decisions. Second, the strict timetables for consultations and panel decisions should provide faster and therefore more effective decision making insofar as justice delayed is often justice denied.

The collection of agreements contained within the framework of the GATT does not establish a single dispute settlement procedure, but rather a number of distinct (although similar) procedures applicable in specific types of cases. Importantly, these GATT procedures examine whether a country is in compliance with its obligations under the GATT – obligations that are often set forth in broad and vague terms which can be subject to a range of interpretation (as well as political and ideological disagreement). In contrast, the FTA dispute-resolution procedures, in large part, will focus on whether a country is in compliance with its domestic law or the FTA. This should circumscribe the room for interpretation since more precise and defined standards will be available. Nevertheless, the most relevant GATT procedures for comparison to those of the FTA are the ones found in Articles 17 to 18 of the Subsidies Code, Article 15 of the Antidumping Code, and Articles XXII to XXIII of the GATT.[32]

One advantage of the FTA dispute-resolution mechanisms is that they should operate more quickly and efficiently than do the

GATT procedures. First, the FTA requires each country to notify and, if requested by the other country, to consult before making changes to its AD/CVD law. Early notice *before* potentially objectionable action is taken provides useful warning that will eliminate possible disputes or expedite the dispute-resolution process if necessary. Neither country need wait for the injurious effect of a new law to be felt before demanding consultations and reference to a binational panel for resolution (Article 1903).[33]

Second, while some of the relevant GATT procedures, such as the GATT Subsidies Code, set a specific time frame for establishing a panel and obtaining a panel decision,[34] they have failed to accomplish timely dispute resolution. Even if the established deadlines do not slip unduly, GATT procedures are susceptible to breakdown after the submission of panel reports because the parties cannot agree on remedial actions. By contrast, the FTA sets out clear time limits for each stage of the panel review process[35] as well as for the time within which remedial action is to be taken.[36] Further, the FTA authorizes the institution of a dispute settlement panel prior to the final determination in a domestic AD/CVD investigation, in readiness for the filing of a formal complaint for binational panel review following the final agency decision (Article 1904.4).[37]

Third, dispute resolution under the FTA will be less cumbersome than under the GATT because third parties cannot intervene in disputes between the United States and Canada. In contrast, under the GATT procedures third parties can significantly complicate and delay any resolution by appearing before a panel or at the time a panel adopts a decision.[38]

Another major advantage of the FTA dispute-resolution process, as opposed to the GATT, is that panel rulings in AD/CVD cases and escape clause actions will be *binding* on the parties and their investigating agencies, and remedial action will be focused on the issues under contention (Article 1904.9). Thus, if the two countries fail to resolve a dispute involving proposed changes to AD/CVD law, retaliation is expressly limited to comparable legislative or executive action (or utlimately withdrawal from the FTA). If no resolution is achieved within the specified period of time for disputes concerning an escape clause measure or other matter affecting the operation of the FTA, the injured party has the right to suspend the application of equivalent benefits under the FTA. The possibility of direct, prompt retaliatory action appropriately limited to the particular matter complained of should encourage mutual resolution and avoidance of disputes. This is preferable to the GATT practice under which parties have greater scope to retaliate in ways that escalate or widen the dispute to encompass areas not originally involved.

Footnotes

1. See *Protocol of Provisional Application to the General Agreement on Tariffs and Trade*, 61 Stat. A3, T.1.A.S. No. 1700, 55 U.N.T.S. 187; *Agreement on Interpretation and Application of Articles VI, XVI and XVIII of the GATT; Agreement on Implementation of Article VI of the GATT*.

2. *Federal Court Act*, R.S.C. 1970 (2d Supp.), c. 10, s. 28(1).

3. The following agency determinations may be appealed to the CIT:

   - decisions not to initiate an antidumping or countervailing duty proceeding
   - decisions not to review agreements to eliminate LTFV sales, eliminate or offset subsidies, cease exports, or eliminate injurious effects
   - decisions not to review a determination on the basis of changed circumstances
   - negative preliminary injury determinations by the International Trade Commission (ITC)
   - determinations by the Department of Commerce (Commerce) that a case is "extraordinarily complicated"
   - negative preliminary LTFV sales determinations by Commerce
   - negative subsidy determinations by Commerce
   - final injury determinations by the ITC
   - final LTFV sales determinations by Commerce
   - final subsidy determinations by Commerce
   - determinations under administrative review of antidumping or countervailing duty orders
   - determinations by Commerce to suspend an antidumping or countervailing duty investigation
   - injury determinations by the ITC during a review of a suspended investigation.

   See 19 U.S.C. § 1516a(a)(2)(B). Note that the AD/CVD binational panels do not have authority to review all of the above determinations. Parties to a section 201 proceeding may currently appeal issues of procedural irregularity, but not the merits of a case. See *Maple Leaf Fish Co.* v. *United States* (1985), 762 F. (2d) 86 (Fed. Cir.).

4. Judicial review in previous U.S. cases involving Canadian products required the following lengths of time: post (CVD) – 2 years, 2 months; sugar and syrups (AD) – 4 years, 5 months; methyl alcohol (AD) – 2 years, 2 months; and iron construction castings (AD) – 1 year, 4 months.

5. *Federal Court Act, supra*, s. 28.

6. The deadlines for the panel in hearing appeals of AD/CVD cases are as follows:
   - 30 days for the complaining party to file its complaint
   - 30 days for the designation of the administrative record and its filing with the panel
   - 60 days for the complainant to file its brief
   - 60 days for the respondent to file its brief
   - 15 days for each party to file reply briefs
   - 15-30 days for the panel to convene to hear oral argument by each party
   - 90 days for the panel to issue its decision.

   The domestic investigating authority concerned would then take action not inconsistent with the decision of the panel, within set time limits that take into account the complexity and difficulty of such action (i.e., whether the investigating authority needs to obtain new factual information). *Canada-United States Free Trade Agreement* (19 December 1987), arts 1904.14 and 1904.8 [hereinafter FTA].

7. A 300- to 315-day deadline for an appeal would have been very helpful, for example, in the recently settled U.S.-Canadian potash AD investigation, *Potassium Chloride from Canada* (1987), 52 Fed. Reg. 32 151 (aff'd prelim.). In this investigation, Commerce gave the U.S. petitioners standing to sue without following the rules provided in U.S. law and the GATT Antidumping Code (Article 4.1). If the FTA dispute-resolution mechanism had been available, Canada would be able to obtain a much faster review of this issue than is likely from the GATT or the U.S. courts.

8. While a party may request three judges to hear a case, this is only done in extraordinary circumstances. See (1982), 28 U.S.C. § 255. In Canada, judges in the FCA sit in panels of three, thus minimizing the problem of idiosyncratic interpretation of the law.

9. An example of the disparate results from decisions by a series of individual judges can be seen in the CIT cases involving "generally available" subsidies. Compare *Carlisle Tire & Rubber Co.* v. *United States* (1983), 564 F. Supp. 834 (Ct. Int'l Trade) ("generally available" subsidies are not countervailable); *Bethlehem Steel Corp.* v. *United States* (1984), 590 F. Supp. 1237 (Ct. Int'l Trade) [hereinafter *Bethlehem*] ("generally available" subsidies are countervailable, except for tax deductions).

   In *Cabot Corp.* v. *United States* (1985), 620 F. Supp. 722 (Ct. Int'l Trade) [hereinafter *Cabot*], one CIT judge rejected the established test that Commerce used to differentiate countervailable subsidies from "generally available," non-countervailable government assistance. Commerce had ruled that the Mexican government's two-tier pricing scheme for petroleum products – with one price for all domestic consumers and a second, higher price for foreign consumers – was not a countervailable subsidy. The CIT stated that the programs at issue were "apparently available to all Mexican enterprises, but in their actual implementation may result in special bestowals upon specific enterprises." *Ibid.* at 732.

   The language of *Cabot* was subject to three possible interpretations. First, if individual recipients of a government program could be identified, *any* benefits they received would be countervailable. Second, even if the individual recipients could be identified, Commerce would have to analyze the operation of the program to determine whether certain recipients benefited more than others. Alternatively, Commerce merely had to confirm that the program was both generally available and widely used. See Hunter & Kubach, "Subsidies and Countervailing Duties: Highlights Since 1984" in D. Riggs (Chairman), *The Commerce Department Speaks 1987* (1987) 491 at 514-15.

   This issue remained unresolved for two years. Then, just a few months ago, three judges of the CIT issued three parallel opinions. In *PPG Industries Inc.* v. *United States* (1987), 662 F. Supp. 258 (Ct. Int'l Trade), the court upheld a Commerce determination that the Mexican government's pricing system for natural gas was non-countervailable because it was both generally available and in fact widely used (even though the export price was much higher than the home market price). In two subsequent cases, two other CIT judges adopted the same standard. See *Al Tech Specialty Steel Corp.* v. *United States* (1987), 661 F. Supp. 1206 (Ct. Int'l Trade); *Can-Am Corp.* v. *United States* (1987), 664 F. Supp. 1444 (Ct. Int'l Trade).

Although the three 1987 CIT decisions substantially clarified *Cabot*, they came too late to spare the Canadian lumber industry. The petitioners in the 1983 *Lumber I* case filed a second petition in May 1986 claiming changed circumstances, based in large part on the *Cabot* decision. Commerce then relied upon the *Cabot* decision to issue a preliminary determination that the government assistance at issue (stumpage) was not nonspecific and thus countervailable. The petition was eventually withdrawn, but only after Canada agreed to impose an export tax or alter its stumpage pricing systems. Problems of this sort could be avoided by the use of five-member panels.

10. Indeed, in the *Cabot* case the CAFC declined to address the merits on appeal. Commerce appealed the 1985 *Cabot* decision to the CAFC, but the CAFC ruled that the order remanding the case to Commerce was not yet a final determination and thus not subject to appeal. *Cabot Corp.* v. *United States* (1986), 788 F. (2d) 1539 (Fed. Cir.).

11. See for example, *Canadian Meat Council* v. *United States* (1987), 661 F. Supp. 622 (Ct. Int'l Trade) (unlawful for Commerce to assume that subsidies provided to swine producers also benefited pork producers); *Alberta Pork Producers' Marketing Board* v. *United States* (1987), 668 F. Supp. 445 (Ct. Int'l Trade) (Commerce determination regarding Ontario Farm Tax Reduction remanded because method of estimation not reasonably accurate); *Washington Red Raspberry Comm.* v. *United States* (1987), 657 F. Supp. 537 (Ct. Int'l Trade) (proceedings remanded to Commerce due to errors in prices used to calculate dumping margins and other adjustments); *No. 87-104*, slip. op. (Ct. Int'l Trade 1987) (affirmed Commerce determination to use constructed value remanded because finding of inability to recoup costs of production over reasonable period of time not supported by substantial evidence); *Badger-Powhatan* v. *United States* (1985), 608 F. Supp. 653 (Ct. Int'l Trade) (where ITC makes a negative determination on some but not all subject imports, Commerce order cannot include all products and Commerce must recalculate margins to exclude data related to noninjurious products); *Chevron Standard Ltd* .v. *United States* (1985), 758 F. (2d) 629 (Fed. Cir.) (Commerce delay

in revoking Canadian exporter's AD order unlawful); *Philipp Bros* v. *United States* (1986), 630 F. Supp. 1317 (Ct. Int'l Trade) (Commerce decision remanded as unlawful because decision not explained on the record); *Bethlehem, supra,* note 9; *Cabot, supra,* note 9 (rejected Commerce's specificity test); *Republic Steel Corp.* v. *United States* (1982), 544 F. Supp. 901 (Ct. Int'l Trade) (Commerce dismissal of petition unlawful).

12. In Canada, the standard for judicial review is so lenient (that is, determinations are highly likely to withstand the minimal scrutiny) that foreign exporters are often disinclined to even apply for judicial review.

13. The FCA remanded agency determinations to the Antidumping Tribunal (precursor to the current Tribunal) in the following cases: *Brunswick International (Canada) Ltd.* v. *Antidumping Tribunal* (1979), 1 C.E.R. 327; *Taiwan Footwear Manufacturers Ass'n* v. *Antidumping Tribunal* (1980), 2 C.E.R. 251; *Noury Chemical Corp. and Minerals & Chemicals Ltd.* v. *Antidumping Tribunal* (1982), 2 C.E.R. 816; *De Vilbiss (Canada) Ltd.* v. *Antidumping Tribunal* (1983), 1 F.C. 706.

14. *See Certain Line Pipes and Tubes from Canada* (1987), Inv. No. 731-TA-375, USITC Pub. 1965; *Frozen French Fried Potatoes from Canada* (1982), Inv. No. 731-TA-93, USITC Pub. 1259; *Chlorine from Canada* (1982), Inv. No. 731-TA-90, USITC Pub. 1249; *Asphalt Roofing Shingles from Canada* (1980), Inv. No. 732-TA-17, USITC Pub. 1060.

15. In a preliminary determination, the ITC inquires only whether a "reasonable indication" of material injury or threat exists. In a final investigation it must find actual evidence of material injury or threat. Thus, while most ITC preliminary determinations are affirmative, they do not prejudice ITC final determinations. For example, of the 12 AD investigations involving Canadian imports that went to the final determination stage since 1980, 5 were terminated. See *Heavy-walled Rectangular Welded Carbon Steel Pipes and Tubes from Canada* (1985), Inv. No. 731-TA-254, USITC Pub. 1691; *Rock Salt from Canada* (1986), Inv. No. 731-TA-239, USITC Pub. 1798; *Egg Filler Flats of Pulp from Canada* (1984), Inv. No. 731-TA-201, USITC Pub. 1577; *Fall Harvested Round White Potatoes from Canada* (1986), Inv. No. 732-TA-93, USITC Pub. 1259; *Certain Fresh Cut Flowers from Canada* (1987), Inv. No. 731-TA-327, USITC Pub. 1956.

Similarly, of the eight CVD investigations that went to the final determination stage, the ITC made three negative determinations (pork, fresh ground fish filets, and miniature carnations). See *Live Swine and Pork from Canada* (1985), Inv. No. 701-TA-224, USITC Pub. 1733; *Certain Fresh Atlantic Groundfish from Canada* (1986), Inv. No. 701-TA-257, USITC Pub. 1844; *Certain Fresh Cut Flowers From Canada* (1987), Inv. No. 731-TA-327, USITC Pub. 1956.

16. For example, the weighted average AD duty was reduced from 17.65 per cent to 6.35 per cent in *Rock Salt from Canada* (1985), 50 Fed. Reg. 49 741 (final affirm.); from 11.3 per cent to 6.8 per cent in *Certain Fresh Cut Flowers from Canada* (1987), 52 Fed. Reg. 2126 (final affirm.); from 16.47 per cent to 9.73 per cent in *Choline Chloride from Canada and the United Kingdom* (1984), 49 Fed. Reg. 36 532 (final affirm.); and from 24.30 per cent to 16.22 per cent in *Certain Dried Heavy Salted Codfish from Canada* (1985), 50 Fed. Reg. 20 819 (final affirm.).

17. FTA, art. 1902.(d). The general nature of the language in the Agreement – the "object and purpose of [the Free Trade] Agreement" – gives a potentially very broad grant of authority to the panels to review changes in U.S. and Canadian AD/CVD law.

18. For example, these provisions would be applicable if the United States were to change its CVD law to classify unemployment insurance as a countervailable subsidy (and specify that the amendment would apply to Canada). See for example, *Certain Fresh Atlantic Groundfish from Canada* (1986), 51 Fed. Reg. 10 041 (final affirm.) (unemployment insurance not a countervailable subsidy). The Canadian government would have the right to prior notification and could invoke the dispute settlement mechanism, leading to a binding determination by the panel.

19. The dispute-resolution mechanism would apply to changes in U.S. law occurring after the FTA went into effect on January 1, 1989. The FTA contains a standstill agreement applying to calendar year 1988, however, which effectively requires the United States not to change its trade laws during that year or, if it does, to compensate Canada for any changes or to free Canada to withdraw from the FTA.

20. Cf., the dispute settlement mechanism in the Israel-United States Free Trade Agreement ((22 April 1985), United States-Israel, XXIV Int'l Leg. Mats. No. 3 at 653), which is similar in

structure. The parties are obliged to consult regarding disputes. Unresolved disputes are referred to a joint committee. Disputes that are still unresolved are then sent to a conciliation panel (*Ibid.* art. 19.1.). The panel's findings, however, are expressly *nonbinding*; it has power to issue a report only (*Ibid.* art. 19.1 (e)). Furthermore, the imposition of AD/CVD duties or review of AD/CVD determinations are expressly excluded from the dispute settlement mechanism.

21. The general dispute-resolution mechanism in the FTA also compares favourably with that of the Gulf of Maine Treaty (*Treaty to Submit to Binding Dispute Settlement the Delimitation of the Maritime Boundary in the Gulf of Maine Area* (29 March 1979), Canada-United States, T.I.A.S. 10204). Although that treaty provides for binding dispute resolution by the International Court of Justice, it contains no explicit sanctions. The same is true of many of the U.S. treaties of friendship, commerce and navigation. See for example, *Convention of Establishment, Protocol, and Declaration* (25 November 1959), United States-France, 11 U.S.T. 2398, T.I.A.S. 4625.

22. The GATT Code Committees, working on a far more theoretical basis, have been able to develop a number of useful common or administrative principles. See for example, *Report to the Committee on Antidumping Practices and to the Committee on Subsidies and Countervailing Measures by a Joint Group of Experts on the Definition of the Word "Related"* (1982), GATT (28th Supp.), BISD 33; *Committee on Antidumping Practices, Understanding of Article 8.4 of the Agreement on Implementation of Article VI of the GATT* (1982), GATT (28th Supp.), BISD 52; *Committee on Subsidies and Countervailing Measures, Guidelines in the Determination of Substitution Drawback Systems as Export Subsidies* (1985), GATT (31st Supp.), BISD 257. They have been unable to agree, however, on substantive matters such as the definition and valuation of subsidies.

23. In the past round of negotiations, negotiators from both countries discovered that 16 months was simply too short a time to allow for the resolution of all areas of conflict between the two bodies of law. The five-year life of the AD/CVD dispute-resolution mechanism, with the possibility of an extension of an additional two years, should provide the necessary time to resolve the conflicts between the two bodies of law and to create political consensus within each country in support of the proposed changes.

24. (1982), 19 U.S.C. § 2251(b) (1).

25. R.S.C. 1970, c. C-41.

26. R.S.C. 1970, c. E-17.

27. For example, in *Stainless Steel and Alloy Tool Steel* (1983), Inv. No. TA-201-48, USITC Pub. 1377 at Table 13, Canada accounted for less than 4 per cent of total U.S. imports; Japan and the Federal Republic of Germany and France, by contrast, accounted for more than 50 per cent of all imports (based on 1982 data). The U.S. trade was nevertheless important to Canada, as Canadian exports of stainless steel and alloy tool steel to the United States totalled about $11.3 million in 1982 (*Ibid.*). The Canadian industry was simply lumped with the others in the investigation.

    In another case, frozen breaded mushrooms from Canada were caught in a section 201 action aimed at canned mushrooms from Taiwan, Korea and China – which went through the CIT and CAFC unsuccessfully. See *Maple Leaf Fish Co.* v. *United States* (1985), 596 F. Supp. 1076 (Ct. Int'l Trade), aff'd (1985), 762 F. (2d) 86 (Fed. Cir.). In that case, the ITC focused on canned mushrooms, which accounted for the overwhelming volume of the subject imports. The ITC did not pay any attention to whether Canadian imports of frozen breaded mushrooms – which were miniscule and arguably a totally different product – should be excluded. See *Mushrooms* (1980), Inv. No. TA-201-43, USITC Pub. 1089. This would not occur under the FTA.

    The ITC has even held itself legally prohibited from excluding from investigations imports from Canada exported pursuant to the *Agreement Concerning Automotive Products Between the Government of the United States of America and the Government of Canada* (the *Auto Pact*). See *Certain Motor Vehicles and Certain Chassis and Bodies Therefore* (1980), Inv. No. TA-201-44, USITC Pub. 1110 at 12, 43-48 and 101-03.

28. Thus, in the *Stainless Steel* case, not only would Canadian goods not have been subject to any duties or quantitative restrictions imposed on other U.S. imports, but the Canadian industry would have been excluded from the case.

    Similarly, Canadian exports that were subject to the following investigations presumably would have been exempted from the section 201 action had the FTA been available at the time: *Apple Juice* (1986), Inv. No. TA-201-59, USITC Pub. 1861 at Table 10

(Canada accounted for 1 per cent of total imports); *Certain Metal Castings* (1968), Inv. No. TA-201-58, USITC Pub. 1849 (although specific data is often confidential, Canada is believed to account for less than 10 per cent of imports of many categories on an aggregate basis); *Non-rubber Footwear* (1985), Inv. No. TA-201-55, USITC Pub. 1717 at A-83 (Canada as part of "all other" category, accounted for less than 4.45 per cent of latest year's imports); *Certain Canned Tuna Fish* (1984), Inv. No. TA-201-53, USITC Pub. No. 1558 at Table 6 (Canada accounted for less than 2 per cent of total imports); *Mushrooms* (1980), Inv. No. TA-201-43, USITC Pub. 1089 at Tables 9 and 12 (Canada as part of "all other" category accounted for less than 2 per cent and 3 per cent of total imports); *Television Receivers, Color and Monochrome, Assembled and Non-Assembled, Finished or Not Finished, and Subassemblies thereof* (1977), Inv. No. TA-201-19, USITC Pub. 808 at Table 12 (Canada less than 15 per cent); *Sugar* (1977), Inv. No. TA-201-16, USITC Pub. 807 at A-17 (Canada as part of "all other" category accounted for only 9 per cent).

29. This could have been important in the 1980 U.S. section 201 case on *Automobiles* if the vote had been affirmative (the vote was 3-2 negative, but could easily have been decided the other way). An affirmative decision would have been based on the injury caused by imports of *small* Japanese cars. Under the standard in the FTA, Canada could have made a persuasive argument that the large "Big Three" cars from Canada were not "contributing importantly" to the serious injury.

The 1986 U.S. case on foundry products also illustrates how one country's exports may be excluded from escape clause actions because they do not "contribute importantly" to the other's industry's import problems. The case was targeted at imports from low-cost less developed countries. The costs of Canadian exporters, however, were generally equal to their U.S. counterparts. Accordingly, their prices did not affect U.S. prices as the lower-cost imports had. Moreover, imposition of the large tariffs requested (which would have been absorbed by the low-cost exporters) would have completely excluded Canadian exports from the U.S. market. Had the ITC made an affirmative determination, any decision to exclude Canadian imports would have been entirely discretionary. Indeed, the ITC would probably not have focused on the issue. Under the FTA it would be required to do so. Since many future escape clause cases in the United States and Canada will presumably be targeted at imports from low-cost countries, this exception from escape clause action for U.S. and Canadian imports that do not "contribute importantly" could prove to be quite valuable.

30. *Western Red Cedar Shakes and Shingles* (1986), Import Relief Determination, 51 Fed. Reg. 19 157.

31. In an extreme case, a complaint against a U.S. export subsidy (the Domestic International Sales Corporation (DISC) tax system) was first heard by a GATT panel in 1973, decided against the United States by the panel in 1976, blocked until 1981, and was not remedied by the United States until 1984. See *United States Tax Legislation (DISC), Report of the Panel presented to the Council of Representatives on 12 November 1976* (1977), GATT (23d Supp.), BISD 98.

32. Article 3 of the GATT Subsidies Code (See *Agreement on Interpretation and Application of Articles VI, XVI and XVIII of the General Agreement on Tariffs and Trade*) provides that each signatory shall be afforded a reasonable opportunity for consultations prior to another signatory's initiating a countervailing duty investigation, as well as during the investigation itself. If this fails, the dispute may be referred to the committee (consisting of representatives from each of the signatories) for conciliation. Article 17 further provides that should the matter remain unresolved, either party may request that the committee refer the matter to a three- or five-member panel. The panel finding is not binding, however. Rather, the panel submits a written report to the committee, which is turn considers the report and makes recommendations to the parties. The sole enforcement provision, should a party refuse to follow the committee's recommendations, is that the committee may authorize appropriate countermeasures.

    Article 15 of the GATT Antidumping Code (see *Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade*) establishes a similar procedure. Article 15 sets forth a procedure involving consultations, followed by conciliation procedures by the committee and reference to a panel if necessary. Although the effects of a panel determination are not established in Article 15, practice has made clear that panel determinations under the GATT Antidumping Code must also be adopted by the committee. Articles XXII and XXIII of the GATT also provide for consultations, followed by reference to the Contracting Parties for a recommendation or ruling. Article XXIII also provides that the Contracting Parties may authorize countermeasures if "the circumstances are serious enough to justify such action" (Article XXIII.2). See also *Agreement on Technical Barriers to Trade*, Article 13(a): Agreement on Government Procurement, Part VII.

33. This provision also allows the FTA (unlike the GATT) to act as an effective forum for resolving disputes concerning the implementation of harmful but temporary measures by the other party. The FTA would avoid the scenario in *Tuna and Tuna Products*, in which the United States prohibited all imports of tuna and tuna products from Canada from August 1979 to September 1980, and a GATT panel report was first adopted in February, 1982. *United States – Prohibition of Tuna and Tuna Products from Canada, Report of the Panel adopted February 22, 1982* (1983), GATT (29th Supp.), BISD 91.

34. See Article 18.2 of the GATT Subsidies Code (a panel is to be established within 30 days of a request and should deliver its findings to the commission within 60 days of its establishment). Compare Article XXIII of the GATT (if no agreement is reached by the parties in a "reasonable" time, the Contracting Parties shall "promptly" investigate) and Article 15 of the GATT Antidumping Code (if the committee fails to resolve the dispute within three months, it shall establish a panel, with no further time constraints of guidance provided).

35. The FTA sets a limit of 300 to 315 days for review of an AD/CVD decision, and a limit of approximately 245 days for resolution of all other disputes. See FTA, arts 1807 and 1904-14. As a result, the FTA should avoid the lengthy procedures often inherent in GATT dispute resolution. In a case involving the Canadian *Foreign Investment Review Act*, for example, more than two years passed between the U.S. invocation of the GATT dispute-resolution process and the adoption of a panel report. See *Canada – Administration of the Foreign Investment Review Act, Report of the Panel adopted February 7, 1984* (1984), GATT (30th Supp.), BISD 140.

36. See for example, FTA, arts 1903.3 and 1904.8.

37. By contrast, under the GATT a party must wait for the final determination before beginning the dispute settlement process. Thus, in *Spring Assemblies* the ITC issued an order on August 10, 1981, banning imports of Canadian spring assemblies; a panel was not established until four months later, and the final report of the panel was not adopted until May 26, 1983. *United States – Imports of Certain Automotive Spring Assemblies,*

Report of the Panel adopted on May 26, 1983 (1984), GATT (30th Supp.), BISD 107.

38. For example, Argentina intervened before the GATT panel in the U.S. complaint concerning Canada's *Foreign Investment Review Act*. *See Canada – Administration of the Foreign Investment Review Act, Report of the Panel adopted February 7, 1984* (1984), GATT (30th Supp.), BISD 140.

V.

Tariffs and Customs Procedures

Tariffs and Customs Rules

William Barreda

In all the publicity and debate surrounding the Canada-U.S. Free Trade Agreement (FTA), the significance of the elimination of tariffs is often overlooked. This is true because tariff issues are traditional trade issues; they are largely technical and they do not raise new, and therefore controversial, concepts. The removal of bilateral tariffs, however, will benefit a larger volume of trade and will provide greater economic benefits to both trading partners than many of the more controversial provisions of the FTA.

Tariffs

Under the FTA, Canada and the United States will eliminate bilateral tariffs on goods by January 1, 1998. Some tariffs will be eliminated with implementation of the Agreement on January 1, 1989; some will be reduced over 5 years through 5 equal cuts, some over 10 years through 10 equal cuts. A few telecommunications products will be eliminated after 3 annual cuts beginning with implementation.

In most cases, tariffs on individual products are cut at equal rates on both sides of the border. The tariffs on import-sensitive products are generally phased out over 10 years, and where possible, the tariffs on products of particular export interest to the other party are eliminated immediately. The tariff cuts are based on applied rates, and so products that are currently duty free remain duty free. Twenty-five per cent, or $30 billion, of trade between our two countries is subject to tariffs. These duties are about 10 per cent for U.S. exports to Canada and about 5 per cent for Canadian exports to the United States.

While well known, the benefits of tariff elimination bear repeating. The removal of tariffs will make it easier for U.S. and Canadian firms to service both markets from either side of the border. As a result, factories may achieve greater economies of scale and avoid wasting capital on multiple facilities. They will become more competitive worldwide. Canadian and U.S. consumers will benefit from lower prices as well as higher quality goods. At the same time, the phased elimination of tariffs should ease the impact of adjustment on workers and firms.

Economic estimates of the welfare gains of the FTA range from roughly $1 to $3 billion, with the bulk of these gains attributable to the elimination of bilateral tariffs.

Rule of Origin

A year ago at this time, Canadian and U.S. negotiators were at an impasse over the rule of origin for the FTA. The United States wanted to follow its current practice. Under it, origin is conferred by a "substantial transformation" into a new and different article of commerce. For a free trade area with Canada, this rule would normally be combined with a rule of preference based on the use of North American materials and direct cost of processing. We followed this approach in our FTA with Israel. It is a tested practice, which the U.S. Customs Service has experience applying.

Canada objected to basing the rule of origin on substantial transformation. Canadian negotiators maintained that, because substantial transformation is a subjective rule administered case by case, it did not provide the degree of certainty that Canada wanted from the FTA. Canada's primary objective was security of access to the U.S. market. Canada wanted to follow its current practice of using value to determine the country of origin. We objected to this proposal because of the difficulty of verification and because of the burden of across-the-board record keeping for U.S. and Canadian businesses.

Responding to the advice of the U.S. Industrial Functional Advisory Committee on Customs as well as other U.S. business representatives concerned about the rule of origin, treasury staff devised a rule based on processing third-country products sufficient to result in a prescribed change in tariff classification under the internationally agreed Harmonized Commodity Description and

Coding System. Many consultations were held with U.S. industry advisors. Treasury staff went through the Harmonized System chapters and decided what should constitute sufficient processing or assembly to confer origin. These proposals were then discussed at length with Canadian negotiators. Both sides held extensive discussion with private sector representatives. After many long hours, the agreed text was completed.

With limited exceptions, this new rule of origin is expected to produce the same results as our substantial transformation principle, but it provides the certainty that Canadian negotiators sought. Our expectation is that once the rules and regulations for this rule of origin are fully set, this rule will be simpler for the private sector to use. A producer will know under what Harmonized System classification he imports and under what Harmonized System classification he exports and so will be able to certify whether his product meets the rule of origin under the FTA. In cases where the producer is not the importer, however, the producer will want the importer to tell him the classification of the imported parts.

Another complication is that for most assembled products, particularly those incorporating parts from numerous countries, a change in the Harmonized System tariff classification alone cannot adequately determine origin. In those cases, a 50 per cent Canadian and U.S. manufacturing test will be applied. This will require a producer to keep data on the cost and origin of his materials and on his direct cost of processing on the factory floor. It will also be necessary that a producer note whenever he switches from a U.S. or Canadian product to an import from another country. I should emphasize that use of this value-content element is limited to the extent feasible because of the record keeping and other burdens it imposes on manufacturers.

Because the new rule of origin for the FTA is a major departure from existing practice in Canada and the United States, we must expect some initial problems before government officials and business representatives become acquainted with the system. Clearly, our first priority in the United States is to join Canada in the adoption of the Harmonized System. The next step for both governments will be the clarification of administrative procedures as well as the education of government officials and business representatives who will be implementing or using the system. This big undertaking must begin shortly to ensure implementation of the FTA on January 1, 1989.

Other Customs Issues

The key remaining customs issues are (1) the elimination of customs user fees on goods, (2) the limitation on duty drawback and related programs, and (3) the ban on duty waiver programs linked to performance requirements (except as specified in the FTA chapter on automotive trade).

User fees. The U.S. customs user fee is assessed on imports to cover the cost of customs administration. The Canadian negotiators objected to the fee as a border measure inconsistent with a free trade area. While U.S. negotiators could not accept this characterization, they were willing to eliminate the fee by January 1, 1994 as part of the overall FTA.

Duty drawback. Both the Canadian and U.S. negotiators recognized that certain types of duty drawback and related programs are inconsistent with the FTA. Programs that return the duty on third-country inputs used in products exported to the other country distort trade and investment decisions by providing better treatment to exports than to goods consumed domestically.

Therefore, we agreed that third-country imports used in goods traded bilaterally would be subject to duties as if they were consumed domestically. Thus, duty drawback for bilateral trade will end January 1, 1994, with limited exceptions (i.e., goods exported in the same condition in which they were imported and for specific categories of goods as mutually agreed). For goods made in U.S. Foreign Trade Zones, duty must be paid on the value of the third-country inputs incorporated into exports to Canada at either the component or the finished product rate.

Performance-linked waivers. Canada maintains a limited number of duty remission programs that are linked to performance requirements. Import duties are waived if a firm exports or produces a given product in Canada. Generally, the firm is entitled to avoid duty payment on imports proportional to the quantity or value of its exports or domestic production. When remissions are linked to exports, the duty remission program is a GATT-illegal export subsidy. When remissions are linked to domestic production, the program distorts trade by creating an artifical preference for domestically produced goods. This preference is inconsistent with a free trade area.

Thus, in the FTA, both parties agreed to eliminate performance-linked duty waivers by January 1, 1998. No new programs will begin after the later of June 30, 1988 or the date of Congressional approval of the FTA.

The Canada-U.S. Free Trade Agreement: Tariffs and Customs Procedures

J. Alec Macpherson

Introduction

The Free Trade Agreement (FTA) between Canada and the United States signed by Prime Minister Mulroney and President Reagan on January 2, 1988, has been characterized as a precedent-setting agreement. It is described as the most sweeping free trade agreement ever signed by sovereign nations, in that it includes concessions on agriculture (virtually excluded in previous free trade agreements) as well as undertakings on the so-called "new" trade issues of services and investment.

This is a perfectly accurate description. Yet, the core of the Canada-U.S. Agreement, the part that will have the most far-reaching impact on industry and consumers in both countries, is the section of the Agreement covering improved access for goods, that is, the tariff elimination schedules and the changes in customs procedures. In other words, the Canada-U.S. Free Trade Agreement is, first and foremost, about the border measures that affect trade in goods and how these measures will change over the ten-year transition period. Thus, epoch-making though it may be, the Canada-U.S. Agreement is well within the tradition established over the last 40 years of international trade negotiations.

There is another sense in which, when examining the Agreement, the trade cognoscenti feel right at home; this is an agreement firmly rooted in the concepts of the General Agreement on Tariffs and Trade (GATT). Of course, in one sense this is a statement of the blindingly obvious; as Contracting Parties to the GATT, both countries are obligated to ensure that the Agreement meets the free trade area provisions of Article XXIV of the GATT. Article 101 of the Agreement thus states the intention of the two parties to establish a free trade area consistent with Article XXIV.

But the link to the GATT is much deeper and, when recognized more widely, may serve to demystify and de-emotionalize some of the arguments about the Agreement. For example, and I will return to this issue subsequently, the constraints which the Agreement imposes on the conditions under which either party can place restrictions on the export of raw material and energy commodities to the other party, have given rise to almost hysterical accusations of "sellout" by the opponents of the Agreement. Yet for 40 years, since Canada became a signatory of the GATT, we have had an obligation under Article XI.1 *not to place any prohibition or restriction*, other than duties taxes or other charges, whether by "quotas, import or export licenses or other measures . . . *on the importation or exportation of any product*" (emphasis added). This stringent general rule in the GATT allows exceptions for circumstances such as, in the case of export controls, "critical shortages of foodstuffs or other essential products," and the usual import issues relating to public morals, national security, etc. In relation to exports of "exhaustible natural resources," Canada and other signatories to the GATT were permitted to put such resources under trade controls for purposes of "conservation," but only "if such measures are made effective in conjunction with restrictions on domestic production and consumption."

Thus, from the perspective of our years as a GATT signatory, the much-criticized provisions of the Agreement on exports of resources can be regarded as simply more explicit statements of obligations we undertook 40 years ago, but which tended to be forgotten by all exporting countries in the commodity shortage paranoia of the 1970s.

In this paper, I propose briefly to describe the provisions of the FTA affecting tariffs and customs procedures and to comment on the implications and, in some cases, the shortcomings of these provisions. To simplify the analysis, I will discuss these subjects under the following headings:

- Elimination of Tariffs and Customs User Fees
- Rules of Origin
- Duty Drawback and Waivers (Remissions)
- Import and Export Restrictions and General Exceptions.

Elimination of Tariffs and Customs User Fees

Under the FTA, Canada and the United States will eliminate by January 1, 1998, all customs duties on products which cross the Canada-U.S. border and which meet the rules of origin set out in the Agreement. There is also provision for an accelerated tariff removal by mutual consent of both countries. Tariffs will be removed either immediately upon the coming into force of the Agreement on January 1, 1989, or in 5 or 10 equal annual reductions beginning on the same date. The exception to this tidy schedule is central office telephone switching apparatus and parts, where the tariff will be reduced in 3 annual installments.

Upwards of three quarters by value of the products now crossing the Canada-U.S. border do so free of duty. Joining that majority on January 1, 1989, will be products such as some unprocessed fish, whiskey, animal feeds, leather, motorcycles, air brakes for freight cars and computers. Tariffs will drop to zero over five years on products like machinery, chemicals, paper and paper products, various building boards, aftermarket auto parts and furniture. On the more sensitive products, such as processed agricultural products, textiles and apparel, steel, autos and original equipment parts and many manufactured products, tariffs will be eliminated over a ten-year period. Products that now trade free of duty will continue to do so between the two countries. In this regard, Canada has undertaken to continue, and possibly expand, the duty exemption for machinery not available in Canada. Both countries have also agreed, with some exceptions, to continue the duty-free treatment resulting from certain temporary suspensions of customs duty.

Finally, both countries have agreed not to impose customs user fees on goods originating in the other country, and in respect of Canadian goods, the United States has undertaken to eliminate its existing customs user fees by January 1, 1994.

It is both easy and tempting to denigrate the tariff elimination of the Agreement by suggesting that it is "no big deal"; as already mentioned, upwards of 75 per cent of trade already takes place between the two countries duty free. But this figure masks the situation that obtains in many industrial sectors where nominal tariffs remain high in both Canada and the United States. It also takes no account of cases where the tariff rates are not high in absolute terms but which, when applied to the value added at the immediately preceding stage of processing, represent barriers of virtually infinite height. The Canadian Synopsis cites one such example: the U.S. tariff of 19 per cent on zinc alloys. There are, of course, many others of this type, and in both countries.

The eventual elimination of remaining U.S. tariffs is an obvious benefit to the rationalization and hence greater efficiency of Canadian production. But we must not forget that the elimination of the Canadian tariff will bring similar efficiency benefits to many Canadian industries, as the tariffs on some of their essential inputs when imported from the United States drop to zero.

It is true that in the process, some branch plants of foreign firms established in Canada solely to get behind high Canadian tariffs may be phased out over time. But subsidiaries of multinationals come in many guises. Many of those originally established to circumvent tariff barriers by producing in Canada for the Canadian market have stayed and expanded to service much broader markets because Canada has become an economical location to produce many goods. The important aspect of the tariff elimination provisions is that they remove a very important disincentive, although by no means the only one, to firms setting up business in Canada to serve the North American market. There will be no tariff and hence the role of the U.S. customs officer in the flow of goods to the United States will be much reduced.

Rules of Origin

Under the Canada-U.S. Free Trade Agreement, as is always the case in free trade areas, the tariffs of both countries applied to goods imported from third countries remain unchanged. It is therefore essential to have a clear understanding of what constitutes a *bona fide* product of the participating countries and hence what products are eligible for the free trade area treatment when traded among the free trade area partners.

The rules of origin in the Agreement are based on the fact that both countries were in the process of altering their existing tariff nomenclatures to conform with the so-called "Harmonized System" negotiated some years ago under GATT auspices. The system is a standardized one, assigning the same numerical headings, subheadings and sub-subheadings to more or less equivalent products in all countries. Further, the system distinguishes, in a reasonably logical manner, among raw materials, semi-processed materials, semimanufactures, parts, components and fully manufactured products.

The FTA accords duty-free treatment to goods crossing the Canada-U.S. border that are wholly the growth, produce or manufacture of either country. When products imported from third countries enter the equation, the Harmonized System classification comes into play; simply put, if an imported good that crosses the Canada-U.S. border must be classified under a different major tariff heading than when it entered either country, then it is thereby considered to have undergone sufficient transformation to be considered a North American product and hence eligible for free trade area treatment. To explain this simple concept, there are, however, some 18 pages in the Agreement setting out the rules governing specific products or classes of products.

In addition, where assembly of manufactured components is an important part of industrial activity, notably the automotive sector, a percentage transformation rule will apply. In such cases, the end products in question will be accorded free trade area treatment if the total of the value of the materials originating in North America plus the direct cost of processing or assembling the products in either country represent at least 50 per cent of the value of the product when exported to the other country. The important concept here is "direct cost of processing or assembling." In simple terms, it appears to mean those "factory floor" costs which can be directly attributed to the processing or assembly operation in question. It does not include general overheads, the cost of doing business or profit. The 50 per cent rule will also be applied, in tandem with the usual rules for specific commodities, when it makes sense to allow free trade area treatment to goods which change from one closely related Harmonized System category to another, but where there should as well be significant manufacturing costs incurred to justify the free trade area treatment.

In general terms, the rules of origin are sensible. At first sight they appear complex, but they are based on a relatively simple principle: if an imported product has undergone sufficient transformation to move it from one major tariff category upon import to another major category upon export across the Canada-U.S. border, then it is a North American good and will be given duty-free treatment. The system means that once an exporter knows what rule applies to his products, his problems are over as long as his sources and processes remain the same. No longer will it be necessary for Canadian exporters to live with the uncertainty of endless hours of arguing with U.S. Customs over the meaning of " substantial transformation," nor face the prospect of years in front of U.S. customs courts to resolve particularly contentious cases. The essentially subjective test of " substantial transformation" has given way to the objective test of a movement from one tariff item to another, qualified in some cases by a "direct cost of processing" test, or in other words, by a fairly clear accounting concept.

As in all negotiations, however, this concession by the United States was achieved at a price. The requirement that North American materials plus direct cost of processing equal 50 per cent of export value is an onerous one. The normal current rule can be illustrated by the regulation applied by the United States to Canadian auto exports to judge whether they qualify for Auto Pact treatment; as long as the value of components or materials imported from third countries represents no more than 50 per cent of export value, the products are considered to be of Canadian origin. This rule allows overhead and profit to be counted toward North American content. The Canadian Synopsis admits that, in the auto sector, the Agreement's rule of origin is equivalent to a 70 per cent requirement under the current standard. It is reasonable to assume that the new rule will be similarly restrictive for other advanced manufacturing sectors. The result of this rule will be to provide a strong incentive, particularly for Canadian manufacturers, to source components in North America, even if these are not the most economical sources, in order to retain duty-free treatment at the Canada-U.S. border.

The Americans were content with a 35 per cent rule in the U.S.-Israel Free Trade Agreement. One wonders why the much more restrictive rule was demanded of Canada. Is it because this was considered necessary to obtain acceptance by protectionist-minded businessmen or Congressmen in the United States?

Finally, the aspect of the rules of origin most open to criticism is that even the relatively restrictive rules already described do not apply to the apparel sector. If fabric from a third country is used in either country to make clothing, that product will be accorded free trade area treatment only so long as specific annual square-yard equivalent quotas in both the United States and Canada have not been exceeded. The U.S. import quota is reportedly some six or seven times the volume of current Canadian apparel exports to the United States. But due to high U.S. tariffs, current export volume is very small and represents only a small percentage of Canadian production. Not only that, but the U.S. quota, when it is finally filled, would apparently represent less than half of 1 per cent of the U.S. domestic demand for apparel. We often hear of the U.S. elephant and the Canadian mouse. In this case, the elephant appears to be the mythical one always terrified of the mouse. The provisions on clothing appear to have very little to do with free trade.

Duty Drawback and Waivers (Remissions)

As is usual in the case of free trade areas, the FTA provides for the phasing out of duty drawback and schemes of similar impact, such as the U.S. Free Trade Zones. Thus, manufacturers in either country who import components from third countries will, upon export of the finished product to the other country, receive drawback (refund) of the import duty up to 1994 only. The rationale for this provision is that, since tariffs against third countries remain unchanged, the continuation of duty drawback would give differential location advantages to industries in Canada or the United States. The main exceptions will be in the case of imported citrus products and imported fabric for use in the production of apparel. To the extent that the tariff quota for apparel made from third-country fabric, as already described, has been filled and subsequent imports are subjected to the most-favoured-nation tariff in either country, drawback of the import duty would be allowed in the country of production.

In respect to waivers (the usual term in Canadian law is "remission"), the provisions of the Agreement fall into two categories, those in the auto sector and those in other manufacturing sectors. In the auto sector, duty waivers linked to export performance must be phased out by January 1, 1998, and must exclude exports to the other party as of January 1, 1989. Production-linked waivers which Canada extended to offshore auto companies establishing production facilities in Canada, must end by 1996 or the date specified in the agreements with the producers, whichever is earlier.

More generally, all duty waivers must be eliminated by January 1, 1998. In addition, both parties have agreed not to establish new waiver programs or expand existing ones after the later of June 30, 1988, or the date on which the U.S. Congress approves the Agreement.

The provisions on drawbacks and waivers were to be expected in the establishment of the free trade area. The European Free Trade Area had analogous provisions to avoid giving undue advantage to industry in one country over industry in others. Similarly, the days were numbered for the special duty remission programs linked to exports to the United States which Canada had extended to the offshore auto producers setting up shop in Canada. They are, in my opinion, export subsidies and, absent the FTA provisions, would almost certainly have led to petition for U.S. countervail action.

In the auto sector, however, the provisions of the Agreement dealing generally with the duty on imports of components or inputs from third countries, give a uniquely privileged position to one large group of companies, namely, those nearly 200 companies listed in Annex 1002.1 as companies already qualified under the Auto Pact. To the extent these companies continue to meet the assembly and Canadian value added provisions of the Auto Pact, they will continue to be able to import components and vehicles duty free from third countries. No other auto sector companies, and no companies in other sectors, will be able to incorporate third-country inputs duty free into their production, even when this product is subsequently exported to the United States. One understands how this result could have came about, given the stated goal of the Canadian side to maintain the Auto Pact provisions and the likely American insistence on limiting these privileges. But the result is, nonetheless, an oddly discriminatory one.

Import and Export Restrictions and General Exceptions

As already indicated, the provisions of the FTA on import and export restrictions are based on and build upon the rights and obligations which both countries have by virtue of being Contracting Parties to the GATT. The GATT imposes a stringent rule prohibiting such limitations except in carefully defined circumstances. The specific exceptions are: in critical shortage situations, where restrictions are necessary to enforce grading or classification standards and for support of domestic agricultural or fisheries stabilization programs. The Canada-U.S. Agreement affirms these provisions in respect of bilateral trade. It further interprets the GATT provisions with the understanding that they should be read as prohibiting minimum export price requirements, and except in the context of antidumping (AD) and countervailing duty (CVD) cases, minimum import price requirements.

In Article XX, the GATT permits the imposition by Contracting Parties of restrictive measures in a variety of circumstances, such as the protection of public morals; the protection of human, animal and plant life and health; the control of prison labour products; the protection of "national treasures" (art, etc.); and the participation in intergovernmental agreements to stabilize the price of internationally traded commodities. The GATT requires that such measures not be imposed in an arbitrary or discriminatory fashion and that they not be disguised restrictions on international trade.

Similar caveats apply to three other circumstances where the GATT allows restrictive measures. These are specifically mentioned and more closely defined in the FTA. The three instances are: (1) the conservation of exhaustible natural resources, *provided* the restrictions are made effective in conjunction with restrictions on domestic production or consumption, (2) restrictions on exports of domestic materials to ensure supplies to domestic industry at times when domestic prices are being kept below world prices as part of a governmental stabilization plan, *provided* the restrictions do not act to increase exports of or the protection afforded to the domestic industry, and (3) measures essential to the acquisition or distribution of products in general or local short supply, *provided* that such measures are "consistent with the principle that all contracting parties are entitled to an equitable share of the international supply of such products."

The Canada-U.S. Agreement permits the imposition of restrictions on bilateral trade in these circumstances so long as: the proportion of the supplies to the other party is not reduced below that which obtained in a representative previous period; the export price is not increased by specific governmental measures; and the restriction does not require disruption of normal channels of supply.

The Agreement continues the "grandfathering" of measures predating the GATT (those covered by the "protocol of provisional application"). Specifically, Canadian and U.S. log export controls, Canadian East Coast fish export controls, the Canadian beer industry and the U.S. maritime industry (by virtue of the continuation of the *Jones Act* provisions) are also excepted from the Agreement.

Apart from these exceptions, the Agreement will require the elimination or phasing out of a range of import controls: by Canada, on used cars and aeroplanes and, once agreed price conditions are met, on wheat, oats and barley; by the United States, on lottery tickets and materials; and by both countries, insofar as bilateral trade is concerned, on all meat goods.

Against the background of this detailed description of the provisions of the Agreement on import and export restrictions, the comment made earlier, that there is not much here that is new or frightening, can perhaps be better understood. As mentioned earlier, under the GATT Canada had already accepted a stringent discipline on import and export controls and had gained important rights in relation to the action of other countries. Admittedly, the GATT rules on such restrictions, particularly as they affect imports, have been among the most ignored of all the parts of the GATT. The fact remains, however, that Canada long ago accepted this obligation.

Further, Canada accepted the obligation that, if export restrictions were applied to conserve exhaustible resources or protect materials in short supply, this could be done only "in conjunction with" domestic controls and, in the case of shortages, taking into account the principle of " equitable share." It is not, therefore, surprising that in the context of the much more extensive trade coverage of the FTA, particularly after the general ignoring of obligations on export controls during the 1970s, the Agreement contains, no doubt at U.S. insistence, more explicit definitions of these concepts. But more explicit definitions serve the interests of the exporting country as well, by narrowing sharply the possibilities for differing interpretations of the GATT's somewhat vague language.

Finally, in the energy field Canada exacted an important additional concession, namely, the much tighter definition of what constitutes national security interests. The lack of a reasonable definition of national security has been a particular bone of contention in the past when the United States had used "security interests" as a reason for restrictive actions against exports of Canadian energy products.

It is therefore difficult to understand why, since the GATT has been an accepted, indeed cherished cornerstone of Canadian commercial policy for the past four decades, the similar, and in some cases identical provisions of the Canada-U.S. Agreement on export restrictions should have aroused such furor and given rise to such purple prose. These are well established trade law principles, admittedly much abused and forgotten in recent years, but old hat all the same.

Conclusion

This, then, is the "border measures" core of the Canada-U.S. Free Trade Agreement. How can one briefly sum up its impact? The tariff deal is arguably the most sweeping ever reached between two major trading countries. It is truly remarkable that no exceptions were found to be necessary; all tariffs will be eliminated. The results for both countries are bound to be positive. The rules of origin are an innovative and essentially simple adaptation of the advantages provided by the standardized approach embodied in the Harmonized System of tariff classification. Nonetheless, particularly since the 50 per cent rule linked to direct cost of processing applies without exception to the huge auto sector, one has to be concerned about the somewhat protectionist cast of the origin rule and the potential for diversion of trade to less economic sources of supply. Finally, the privileged position retained by the "Old" Auto Pact companies is an odd component in a free trade agreement.

All this said, however, the Agreement's border measures provisions have good parentage (the GATT), are in general terms sensible, and should have far-reaching positive effects in North America.

VI.

The National Treatment Commitments

Policies for the Treatment of Foreign Participation in Financial Markets and their Application in the U.S.-Canada Free Trade Agreement

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Introduction/Regulatory Context

The financial sector of a country plays a unique role by allocating financial resources to enable the real economy to operate effectively. The regulatory framework for the financial sector must ensure that the allocation process is efficient and, at the same time, protect the safety and soundness of the financial system itself and the financial resources entrusted to it. The ability of a country's central bank to conduct monetary policy is influenced by the nature of the financial sector. Thus, the financial sector is typically more closely regulated than other sectors of an economy. The financial health of individual firms and the avoidance of conflicts of interest between them are important objectives of the regulatory framework. Since financial intermediation involves the holding of customer deposits in trust, and market intermediation involves investor protection, the regulatory framework must ensure confidence in the financial sector.

In both the United States and Canada (as well as in other countries), the regulatory framework has strongly influenced the organization of the financial sector. Three underlying elements of a national regulatory framework can be considered – functional, jurisdictional, and foreign ownership – all of which were important considerations in the U.S.-Canada financial services negotiations.

The functional element refers to the organization of the intermediation function. In many countries, both the financial and market intermediation functions can be employed within a single institution. Historically, both Canada and the United States have had systems in which this was not the case. In the United States, the *Glass-Steagall Act* was passed in 1933 to separate commercial banking from investment banking activities. Commercial banking is also separated from commercial (i.e., nonfinancial) activities and the insurance and real estate businesses. Over time, commercial banks have made numerous inroads into the securities business and *vice versa*, and new legislation may allow affiliations between commercial banks and investment banks. Market developments also have resulted in affiliations between commercial entities, insurance and securities firms, such as General Electric with Kidder Peabody and Sears with both Allstate Insurance and Dean Witter.

In Canada there evolved a system of "four pillars" which was reflected in the *Bank Act* of 1967 and other financial statutes that had separated commercial banking, investment banking, insurance, and the trust and loan business. As in the United States, market developments and technical innovation had, over time, blurred much of the distinction among the pillars. Canada's new financial sector policy (presented in Minister of State Hockin's "New Directions for the Financial Sector"), which is being implemented in stages, will allow affiliations among firms from the various pillars. On the other hand, a new policy will establish barriers between commercial firms and financial firms (except for securities firms). Thus, transactions such as Imasco's acquisition of Canada Trust and Brascan's ownership of Trilon would not be allowed in the future.

The second important aspect of a national regulatory framework for the financial sector is jurisdictional. In federal systems such as Canada and the United States, subnational governments participate in the regulatory process. In Canada, the provinces regulate the securities industry; the federal government regulates the banks, and both levels of government regulate the insurance and trust industries. In the United States, the states regulate insurance companies; the federal government has the primary responsibility for regulating securities firms, and both the states and the federal government regulate commercial banks. Even at a particular level of government there can be numerous jurisdictional authorities. While Canada has recently rationalized its federal regulatory system by combining the Office of the Superintendent of Insurance with the Inspector General of Banks, the United States maintains several bank regulatory authorities at the federal level.

Finally, the treatment of foreign-owned firms within a national financial system is an important separate element of the regulatory framework for the financial sector. Through direct investment, i.e., by establishing a presence in a foreign country, foreign financial firms seek to provide financial services within a domestic market and to compete with domestic financial institutions.

Several questions immediately become relevant. Should foreign financial institutions be allowed to enter a country and establish there? In fact, should they be *required* to establish in a country in order to offer a financial service to a resident of that country? If they can enter, in what corporate form – a branch of the parent firm, equity investment in an existing firm, or a wholly owned subsidiary incorporated in the host country? Once allowed into the country, should there be restrictions on the operations of the foreign firm different from those applied to domestic firms?

In the United States, foreign banks, securities firms and insurance companies are allowed to enter in their organizational form of choice. Many of the major U.S. stock exchanges and some states, however, require a subsidiary form rather than a branch for securities firms and insurance companies respectively, in order to receive full benefits. Once established in Canada, the foreign firms are treated essentially the same as domestic firms. In Canada, subject to a screening process, foreign banks may enter through a wholly owned subsidiary, and foreign securities firms will be able to enter as a wholly owned subsidiary or by equity interest in a domestic firm. Foreign insurance companies may enter as a branch of the parent or as a wholly owned subsidiary. Once established, foreign insurance companies are treated largely the same as domestic firms. Foreign securities companies are in the process of achieving that status. Foreign banks, however, are not treated the same as domestic banks.

When two or more countries begin to negotiate a common financial services agreement, these three elements – functionality, jurisdiction and foreign treatment – become key considerations, especially when the countries differ in each aspect. Is there a common intersection between the two countries' regulatory frameworks that can accommodate each country's basic regulatory regime? Or, does one country have to alter its regime dramatically in order to obtain a common agreement with the other? Is there a model for treating foreign firms that makes it easier to reach agreement?

These were the questions that had to be answered in the context of the negotiations of the financial services aspect of the U.S.-Canada Free Trade Agreement (FTA). At the outset, there was tacit agreement that, ideally, each side should be able to determine the structure and functional organization of its own financial sector. Similarly, the negotiators acknowledged the legitimacy of each country's distribution of regulatory authority and implicitly agreed that ultimately, negotiations – while initially seeking to accurately describe and explain all aspects of the two financial systems – would focus on the federal governments and their ability to influence the regulatory environment either directly or by working with relevant state and provincial authorities. Within these parameters, the negotiators undertook to address the treatment of foreign ownership and activities in the financial services sector. This paper will focus on the possible models for treating foreign ownership and discuss the text of the relevant portions of the Free Trade Agreement.

Models for Treatment of Nonresidents

There are two main sets of models governing the treatment of foreign-owned financial institutions: discriminatory policies and national treatment rules. Discriminatory models will be considered first.

Infant Industry

One approach to the treatment of foreign firms, often adopted by less developed countries and less frequently adopted by industrialized nations, is referred to by economists as the "infant/senescent" industry argument. Under the infant industry policy, domestic firms are protected by special benefits or by excluding foreign firms altogether. The purpose is to give domestic firms an unspecified "grace period" during which they are expected to develop expertise and financial strength while being spared the competition of foreign firms. At some point in the future, the domestic firms are expected to reach large enough economics of scale to successfully face competition from foreign firms. Countries which have adopted this policy have generally faced two problems: domestic firms have taken advantage of the lack of competition to obtain large economic rents rather than grow and it has been difficult to decide when the restrictions on foreign firms should be lifted. The senescent policy is a variant, but is applied when a domestic industry has become uncompetitive and needs protection in order to rationalize and grow again.

The infant industry policy was adopted by the Province of Ontario for its securities industry from 1971 until June 30, 1987. During this period, new foreign firms were prohibited from entering the full-service securities industry; existing foreign firms were allowed to remain in a grandfathered status, but their growth was limited to the average of the largest domestic firms in order that competition from them would not threaten the domestic firms. Effective June 30, 1988, Ontario will have switched to a regulatory model of full *de jure* national treatment for foreign firms (although the federal authorities could continue to frustrate the policy if they apply the policy of reciprocity on entry). Ontario eased the adjustment for domestic firms to competition from foreign firms and effected a bias toward Canadian control of the industry by delaying the entry of foreign firms for one year and, with the cooperation of the federal authorities, by allowing Canadian banks the first opportunity to acquire securities firms.

An infant industry policy is not an effective model to adopt for negotiating an agreement in financial services. The country without the policy would be reluctant to "pay" concessions to end the discriminatory practices. Contrary to the Canadian press commentary in December 1986 about "lost bargaining chips" following Ontario's announcement of the liberalization of their securities industry, this infant industry model would not have been an effective bargaining chip against the U.S. side in the negotiations.

National Security/Strategic Industry

The next discriminatory model is the national security or strategic industry case. Irrespective of the economic costs, this policy is justified by the strategic or political role that an industry might provide a country. This argument has been used for the U.S. maritime industry and the Canadian cultural sector. A weakened version has sometimes been advocated for the Canadian banking sector. Because of the noneconomic nature of this policy, economists have generally accepted this model as is. This policy, however, does not advance the case for an agreement which removes barriers.

Strict Reciprocity

Another discriminatory model, the policy of reciprocity, has occasionally contributed to trade liberalization and has a "common sense" popularity in some countries. Under this policy, foreign financial institutions have a disadvantage or face the possibility of a disadvantage in the host country *vis-à-vis* domestic institutions in their entry or treatment after entry. The host country offers the possibility of entry or improved treatment to foreign firms in exchange for improved treatment for its own firms in the home country of the foreign firm. Authority to employ this policy has been adopted by Canada and other countries for their financial sectors. For example, while the word "reciprocity" is not used, section 8(d) of the Canadian *Bank Act* prohibits the issuance of a bank charter to a foreign bank subsidiary unless "the Minister is satisfied that . . . treatment as favourable for [Canadian] banks . . . exists or will be arranged in the jurisdiction" of the foreign bank.

While the goal of a strict reciprocity policy may be to force the opening of other markets or the adoption in other markets of a similar regulatory structure, the policy has the potential to backfire. When two countries with diverse functional regulatory regimes adopt strict reciprocity policies toward one another, several negative results are possible. If one country is stronger or a relatively more important market for the other, the stronger country might try to unilaterally impose its regulatory regime upon the other. Alternatively, a stalemate might occur, and each country will incrementally take benefits away from firms of the other country until the lowest common denominator is reached. When applied on a multilateral basis, the problem is compounded and an additional administrative burden emerges, namely the monitoring and, to some extent, the emulating of the regulatory regimes of all other countries. Also, a strict reciprocity policy can be somewhat vague in relation to the interpretation of "treatment as favourable" and of which factors to take into consideration when applying the policy. The result can be the imposition of many new barriers.

The *Bank Act* reciprocity policy has not been a problem for the entry of U.S. bank subsidiaries into the Canadian banking industry because there is no barrier to the entry of foreign banks in the United States. During the course of the U.S.-Canada Free Trade negotiations, however, certain persons in Canada advocated the use of a reciprocity policy to prevent the entry of U.S. bank subsidiaries and U.S. securities firms into the Ontario securities market. Their rationale, involving the treatment as favourable notion, concerned the inability of Canadian banks to enter the securities business in the United States. The proponents of the reciprocity approach argued that the United States should eliminate its *Glass-Steagall* regime or at least exempt Canadian firms from its coverage, since Canada was in the process of eliminating equivalent laws. Alternatively, it was argued that U.S. banks should not be allowed to engage in those activities in Canada denied Canadian banks in the United States. The United States argued that it could not change its entire regulatory regime to accommodate Canada. The alternative of exempting Canadian banks would mean better treatment for them than that given U.S. banks in the United States, certainly a perverse situation since the most that U.S. banks could expect in Canada would be almost equal treatment.

This situation derived from the growing incompatibility of the functional regulatory framework of the U.S. and Canadian financial sectors. The use of a reciprocity policy by both the United States and Canada toward one another could have resulted in a worse situation. To counter Canada's use of reciprocity to discriminate against U.S. securities firms, the United States, for example, could have mirrored many of Canada's discriminatory banking laws, such as the prohibition on entry as a branch of the parent, and restrictions on capital growth and market share. This would have resulted in no agreement in financial services and a situation worse than the *status quo*. Clearly then, the application of a strict reciprocity model does not provide an appropriate basis on which to conclude a successful agreement in financial services.

Equality of Access

Another discriminatory model, one of selective reciprocity, can be referred to as the "equality of access" policy. This policy is a limited version of the strict reciprocity policy. It was proposed by some observers as an alternative to either a strict reciprocity model or a national treatment model in the financial services sector. Equality of access limits itself to questions of entry, not treatment after entry. The Canadian policy would be that U.S. banks and securities firms would be allowed entry into Canadian financial markets on the same basis that Canadian banks and securities firms are allowed access to U.S. financial markets. Since the only restriction in the U.S. market is cross activity (i.e., no banking into securities and *vice versa*), that restriction would apply to U.S. firms entering Canada. If the U.S. applied the same policy to Canadian firms, however, the result would be prohibition on the entry of Canadian banks as branches into the United States. Again, an agreement concluded on this basis is less than optimal.

If discriminatory policies in both countries do not result in successful agreements, are national treatment policies any better? There are two national treatment models to consider, "*de jure*" and "equality of competitive opportunity."

De Jure National Treatment

The *de jure* national treatment policy is generally used in trade law and in the investment area in Friendship, Commerce, and Navigation Treaties negotiated by the United States over the last two hundred years. The Services Chapter, (Article 1402(1) of the FTA), contains a typical wording of the policy: "each Party shall accord to persons of the other Party treatment no less favourable than that accorded in *like circumstances* to its persons . . ." (emphasis added). A national treatment policy has a major advantage over discriminatory policies in that it requires only the equitable application of a given jurisdiction's laws and regulations to its own residents and nonresidents. It is thus easier to administer than a policy of reciprocity, which may involve the application of a variety of rules and regulations to foreigners, as determined in part by their treatment of nonresidents in their countries. The results of a national treatment policy in trade and investment are generally accepted by economists to lead to increased exports and inflows of capital, with correspondingly greater economic benefits.

Nevertheless, when a policy of *de jure* national treatment is applied to the service sector of a country, including the financial sector, at least three problems arise. First, given the regulatory nature of financial and nonfinancial services industries, identical treatment applied to both domestic and foreign-owned firms could, in fact, be more onerous on the foreign firm, for example, the application of accounting standards to foreign firms. U.S. banking law recognizes the different regulatory regimes in other countries with respect to accounting standards, and provides for some leniency to foreign firms to accommodate the different practices.

Secondly, there may be cases where the *prima facie* treatment of foreign firms would appear to be more restrictive, but has been adopted for prudential reasons, as might be the case for deposit or collateral requirements on foreign firms not legally established in a country. The Services Chapter explicitly recognizes this latter problem and allows different treatment for prudential, fiduciary, health and safety, or consumer protection reasons (Article 1402(3)).

The third potential problem with *de jure* national treatment concerns the ambiguous notion of "like circumstances." In fact, this has caused some problems in the financial services area. As the U.S. Treasury reported to Congress in its various National Treatment Studies (1979, 1984, and 1986), the use of the like circumstances notion in *de jure* national treatment can result in or condone what would otherwise be considered restrictive practices. For example, consider a country that has never permitted the entry of foreign banks which now passes a law that prohibits the creation of any new banks. Since the law applies equally to foreign and domestic persons, it could be argued as *de jure* national treatment. Consider another law which states that no domestic or foreign person can own more than 10 per cent of a financial institution. While the treatment is the same, clearly a foreign-owned firm would never have the opportunity to compete in the host country. Finally, consider the situation in the Canadian financial sector which caused problems for the U.S. negotiators. Any bank with closely held ownership is considered to be a Schedule B bank. All foreign bank subsidiaries in Canada, by definition, are closely held by their parent; therefore, they must be Schedule B banks. Since all Schedule B banks are in "like circumstances," it is possible under *de jure* national treatment for discriminatory laws to be passed that apply only to Schedule B banks.

Such an argument was made when the 1980 *Bank Act* established an 8 per cent asset ceiling for all Schedule B banks.

Equality of Competitive Opportunity

We believe that the problems with *de jure* national treatment are overcome by the national treatment model called "equality of competitive opportunity" (ECO). This concept is embodied in the U.S. *International Banking Act* of 1978 and has been U.S. policy in the financial sector ever since. The policy focuses on whether opportunities exist for a foreign firm to compete on an equal basis with domestic firms in the domestic market. As such, it incorporates the concept of right of establishment and the possibility of different regulatory treatment to achieve the opportunity for competition on an essentially equal basis. Applied to Canadian firms, ECO states that a Canadian bank should have the opportunity to establish in the United States in its corporate form of choice and, once established, should have the opportunity to compete with a U.S. bank on an equal basis, even if it requires *prima facie* a more lenient treatment of the Canadian bank. It is on this basis, for example, that Canadian banks have been able to enter the U.S. market as a branch of the parent, even though there are no like circumstances to consider in terms of U.S. branches within the United States.

Comparing the models for treatment of foreigners from the standpoint of their potential influence for liberalization, we believe that equality of competitive opportunity offers the best prospects. None of the discriminatory policies, if adopted by both parties and pursued unswervingly, offer anything better than the *status quo*. Indeed, the infant industry and national security models could be used to increase discrimination. The strict reciprocity model might lead to liberalization, but only with the unlikely and unsatisfactory imposition of a less discriminatory regime by one country (presumably larger and more powerful) on the other (which is weaker and will inevitably be obliged to accept the former's approach). While *de jure* national treatment might result in eventual liberalization, it implies a certain rigidity and legalistic posturing that, as pointed out, could, in fact, be used to introduce or perpetuate subtle discrimination. Only an approach which is aimed at pragmatic and effective equality of competitive opportunity is sufficiently flexible in order to permit ongoing reduction of discrimination and improved compatibility of regulatory regimes, while preserving the independence of each country's regulatory system.

The Financial Services Chapter of the FTA

The Financial Services Chapter of the Free Trade Agreement covers all current and future laws, regulations, and practices relating to financial institutions in both countries. Financial institutions include commercial banks; investment banks; trust, loan/savings and loan institutions; as well as other institutions so designated under the laws of each country. Moreover, financial services cover the right of insurance companies to diversify or establish subsidiaries through acquisition. Financial services offered by nonfinancial institutions and strict insurance services are covered elsewhere in the FTA.

The domestic assets of foreign bank subsidiaries operating in Canada (the closely held or Schedule B banks) are currently limited to 16 per cent of all domestic assets of the Canadian banking system. Foreign bank subsidiaries also face individual capital limits and other restraints such as the sale of loans to the parent bank. Under the FTA, U.S. commercial bank subsidiaries will be exempt from the current restrictions on market share, asset growth and capital expansion, in the same way that Canadian banks are free from these restraints. U.S. commercial banks will also be allowed to establish or acquire securities firms or federally-regulated Canadian insurance and trust companies in the same manner as Canadian banks.

Existing statutes and the initial proposals for financial market reform in Canada contain a major disadvantage for foreign firms, particularly insurance companies. The so-called "10/25" rule, found in many of the federal and provincial statutes governing financial institutions, explicitly prevents a nonresident from acquiring more than 10 per cent ownership of a Canadian insurance, trust or loan company; total nonresident ownership is limited to 25 per cent. The rule is also found in the banking industry, but the 10 per cent limit applies to both Canadians and nonresidents. Similar restraints on acquisition of investment dealers were lifted by Ontario in 1987. However, the federal reform proposals leave the 10/25 rule unchanged.

Under the Financial Services Chapter of the FTA, the discriminatory rules at the federal level will be waived for U.S. firms. Therefore, U.S. insurance firms and other financial companies will have the same rights as their Canadian counterparts to diversify in the financial sector by establishing or acquiring federally-regulated insurance companies, trust companies, Schedule B banks or securities firms. In addition, the Investment Chapter places a standstill on the 10/25 rule in the provincially-regulated insurance industries, so that no province may introduce such a rule in the future (note: Quebec is the only province which currently maintains a 10/25 rule in its insurance industry).

As noted above, Ontario, Quebec and other provinces have opened their securities markets to foreign investors. On the other hand, the federal government interjected, for the first time, in the review of securities firms and implemented a policy based on reciprocity. The result was postponement and delayed approval of applications for entry by U.S. securities dealers and banks. Under the FTA, these applications will be reviewed on a prudential basis, just as for Canadian firms, rather than on a reciprocity basis. U.S. securities firms established in Canada will be able to diversify through a holding company structure into other financial activities such as banking and insurance.

Under the FTA, the United States made a number of specific commitments, although there were no barriers to national treatment to eliminate in the United States. The United States agreed to guarantee the right of Canadian banks to retain their multistate branches that were grandfathered under the *International Banking Act* of 1978, resulting in Canadian banks receiving better than national treatment *vis-à-vis* U.S. banks. If the *Glass-Steagall Act* is amended, the United States has committed itself to extend these benefits to Canadian financial institutions in the United States. Such guarantees have never before been extended to any country.

The United States responded to Canadian concerns regarding the treatment of their banks and securities firms which merge in Canada – but have operations in the United States – by agreeing to allow Canadian banks (as well as U.S. and other foreign banks) in the United States to underwrite and deal in debt obligations fully backed by Canada or its political subdivisions. This is a new power that is consistent with the existing ability of banks to underwrite and deal in securities of the U.S. Government and its political subdivisions, yet does not undermine the basic tenets of the *Glass-Steagall Act*. Moreover, this privileged treatment of Canadian debt instruments is enjoyed by no other country.

This new power enables Canadian firms to take advantage of liberalization in Canada, while retaining their most important securities activities in the United States. One of the side effects of this new power will be a direct benefit to the federal government, the agent Crown corporations, the provincial governments and the municipal governments in Canada. Since their debts will be underwritten and traded by more firms in the United States, the FTA offers the potential for a wider, deeper market and, therefore, lower borrowing costs.

In addition to these specific commitments, both the United States and Canada have made general commitments. The United States has agreed to continue the current treatment provided to Canadian financial institutions established in the United States so long as Canada continues to liberalize its financial markets and extend the benefits to U.S. financial institutions established in Canada. Canada has made an analogous commitment. The Agreement establishes a formal consultative mechanism between the United States Department of the Treasury and the Canadian Department of Finance to oversee this liberalization and deal with any other financial services issues. These measures represent broad commitments on the part of the two countries, and are consistent with the manner in which finance ministries typically conduct relations with one another.

Analysis of the Text

Any negotiation can be successfully concluded in one of two ways: "equal concessions" or "equal results." If both countries have comparable restrictions, such as tariff barriers on both sides of the border, then an agreement concluded on the basis of equal concessions can be considered equitable. If the restrictions are unequal, however, then an agreement based on equal concessions is fundamentally unbalanced. In a negotiation where one side, such as Canada, has a discriminatory regime, it is inequitable for the other party, the United States, to pay for the removal of barriers, since otherwise there would be an incentive for the United States to discriminate against Canadian banks and securities firms immediately before the start of the negotiations, and then ask for special favours to lift the discrimination. Had both parties approached the negotiations on this basis, the result would have been a lose-lose agreement.

As with any agreement, compromises had to be made. The United States was unable to convince Canada to adopt a regime of equality of competitive opportunity in its financial sector, including the right of entry as a branch of the parent bank. Canada was unable to convince the United States to adopt a regulatory regime similar to its own or to obtain an exemption from *Glass-Steagall* for its firms.

Paragraph 4 of Articles 1702 and 1703, which provides for symmetric commitments of the two countries, is an example of a compromise; yet, it is carefully worded to incorporate some powerful features. The U.S. commitment to "continue to provide Canadian-controlled financial institutions . . . with the same rights and privileges they now have in the United States market . . ." continues the U.S. policy of national treatment in terms of equality of competitive opportunity. Once the rollback provisions of Articles 1703(1) to 1703(3) are implemented, the Canadian commitment to "continue to provide United States-controlled financial institutions . . . with the same rights and privileges they now have in the Canadian market . . ." is a standstill as well as a commitment to liberalize in a nondiscriminatory way.

Since paragraph 4 refers to "established" firms only, Canada maintains the ability to prohibit the entry of branches of a U.S. parent bank. At the same time, the United States has not given up its right to continue to consider this a barrier, and has made no commitment with respect to U.S. branches of Canadian banks since these are not established under U.S. law (not to be confused with multistate branches which are). Paragraph 4 also contains a broad commitment to liberalize, which allows flexibility on both sides. There is incentive to liberalize, since the current treatment to established firms of the other side is guaranteed only so long as the other party continues to consult and liberalize, and to extend the benefits of such liberalization.

The other area of compromise concerns the definition of "financial institution", which may seem technical, but is key to the chapter since almost all of the obligations of the two countries are made with respect to the treatment of financial institutions. The financial sector laws in Canada are limited in number and are carefully defined in scope. The laws covering the financial sector are institutionally based, rather than functionally based, so that it is possible for nonfinancial institutions to offer financial services. The U.S. laws are broader in scope so that any institution offering a financial service might be considered a financial institution. The Agreement allows each side to continue its current practices of defining a financial institution.

Regardless of the compromises, both countries obtained important benefits from the financial services agreement which they might not have been able to obtain otherwise. The guarantees for the future are important, as well as the new atmosphere of cooperation and consultation that will characterize the two countries' relations in the financial area. For example, during the course of the negotiations, it became apparent that the U.S. Treasury could have some influence in certain immediate issues – i.e., good faith – rather than waiting until the end of the negotiations. The State of Wisconsin was considering regulations which would have had the unintended effect of discriminating against foreign-owned banks including a Canadian bank whose home state was in the Midwest Regional Compact. After Treasury talked with the Wisconsin regulators, they agreed to make the necessary changes in May 1987. In another situation, in August 1987, the Commodities Futures Trading Commission agreed to implement regulations affecting Canadian options and futures in which a Canadian stock exchange had had an interest for several years. These are examples of the way in which U.S. and Canadian financial institutions can benefit from free trade, especially under the new consultative mechanism established under the Agreement.

Relationship of the Financial Services Chapter with the Overall FTA and Other Agreements

A question frequently asked about the FTA concerns the relationship between Part Five on Financial Services and Part Four on Services, Investment and Temporary Entry, and why the chapters on services and financial services are so different in character. As discussed in the first section above, the financial sector has a unique role in the economy, and it often involves questions of monetary policy. Policies that may apply to imports or exports of potatoes or even cross-border transportation services do not necessarily work for, and should not be forced upon, international agreements pertaining to financial services.

Furthermore, in contrast to the nonfinancial services sector, the major issues of interest in financial services negotiations did not involve the export and import of financial services, but rather direct investment questions. For example, U.S. securities firms "export" financial services to Canadians in the form of financial advice and the underwriting of Canadian securities. U.S. residents "import" financial services from Canada through, for example, the services offered by Canadian insurers. The most important aspect of financial services is not, however, trade in services, but capital movements, in particular, long-term equity investment. A major element in the Services Chapter is the right to not establish in order to provide a service, i.e., the ability to provide a service cross-border. Regulators are generally reluctant to support this right in the financial sector for prudential reasons. Responsible regulation of the financial sector requires regulation of individual firms, which would be difficult if no presence – either as a branch or a subsidiary – is required in order to offer the financial service. The elimination of the Ontario exempt market and the requirement for universal registration and a presence in Ontario is an example of this attitude on the part of the Ontario regulators.

There are four additional major reasons which account for the differences in character between the Services/Investment Chapters and the Financial Services Chapter: definition of national treatment, standstill versus rollback, state and provincial coverage and the dispute-settlement mechanism. The definition of national treatment used in the Services Chapter (*de jure*), is fundamentally different from that used in financial services (equality of competitive opportunity). As explained above, *de jure* national treatment would not be effective in the financial sector. Secondly, the Services Chapter was approached from the perspective of a standstill of existing discrimination in both countries. In the Financial Services Chapter a rollback was necessary, given the difference in relative openness of the two countries' financial sectors.

Once a decision was made for a rollback rather than a standstill, the question of subnational coverage became a very difficult issue. The United States felt that it would be politically costly for both parties to force legislative changes in existing state and provincial laws. Also, the benefits of doing so were not that great. From a national treatment point of view, only the Quebec insurance laws and the Ontario trust and loan statutes were restrictive at the provincial level. In the United States, the Midwest Regional Compact proved difficult to Canadian banks, but that problem was solved during the free trade negotiations.

Finally, we come to the question of the dispute-settlement mechanism. First, the United States questioned the need for such a mechanism, given the relatively few disputes in the financial area and their low profile compared to the bilateral trade and investment disputes of the past. Second, and more importantly, the United States questioned the appropriateness of a potentially binding mechanism by trade representatives who do not have the necessary expertise and knowledge of laws and practices in financial matters. Of special concern to U.S. and Canadian financial regulators was the dual body of precedent that would be created by a dispute-settlement mechanism of this type. For example, had the dispute-settlement mechanism applied to financial services, a Canadian-owned bank – but not a U.S.-owned bank – would have had the right to appeal a decision by the Federal Reserve Board to the U.S.-Canada Trade Commission, chaired by the trade ministers. This would make it possible for a U.S. central bank to be overruled by the commission. Moreover, the U.S.-owned bank could appeal the same decision to the U.S. courts, with the possibility of two contradictory decisions being handed down.

The authors feel that this hypothetical situation would create uncertainty and instability in the financial markets, and that the Financial Services Chapter is a better agreement without the overall dispute-settlement mechanism. In its place is a formal consultative mechanism between the U.S. Treasury Department and the Canadian Department of Finance. This mechanism should be able to resolve all disputes. If not, as noted above, paragraph 4 of Articles 1702 and 1703 contains a built-in incentive for the parties to resolve disputes.

Chapter 17 (Financial Services) has also been carefully coordinated with Chapter 15 (Temporary Entry for Business Persons) and Chapter 16 (Investment). Chapter 15 allows temporary entry of financial services personnel, and so complements the capital mobility of financial firms under Chapter 17. Chapters 16 and 17 divide the obligations with respect to direct investment. Chapter 17 covers investments in the commercial, investment and trust banking industries (as well as the 10/25 rule in the federally-regulated insurance industry); the Investment Chapter covers all other industries.

The United States has negotiated Bilateral Investment Treaties (BITs) and Friendship, Commerce, and Navigation Treaties (FCNs) with a number of countries, and these treaties had an important influence on the U.S. negotiating position on the Financial Services Chapter of the FTA. While the banking industry (though not the securities industry) is exempted from the national treatment obligations of the FCNs and the BITs, it is subject to the Most-Favoured-Nation (MFN) clauses. And, while Article 24 of the General Agreement on Tariffs and Trade (GATT) allows free trade area agreements in which MFN treatment is not granted to third parties, the article does not apply to services. Thus, to conform with the obligations of FCNs and BITs between the United States and other countries, any concession given to Canadian firms had to be given to firms from other countries. This is one reason why the new power to underwrite and deal in debt obligations fully backed by the Canadian government or its political subdivisions (Article 1702) was extended to all banks. Canada has no FCN or BIT with any country, and was therefore not so constrained in its commitments.

Finally, a brief comment is in order concerning the relationship between the financial services agreement and the OECD Code of Liberalization of Capital Movements. Under the Agreement, no barrier has been raised to third countries. The immediate changes that will take place in Canada, and both countries' commitments to liberalize further their financial markets, are in perfect accordance with the Code.

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An Analysis of Chapter 16: Investment

J. Christopher Thomas

Introduction

The subject of foreign direct investment has long been controversial in Canadian politics. Foreign investment is often lauded for its employment and wealth-generating effects and at the same time criticized for undermining Canadian policy autonomy. The latter allegation appeals to many Canadians and has formed the basis for federal legislative initiatives such as the *Foreign Investment Review Act* (FIRA)[1] and the National Energy Policy. Even the present government's investment policy, which was intended to repudiate the excesses of the FIRA, nevertheless reflects a cautious approach to the issue. Although Investment Canada was created to encourage foreign investment, it also screens investment, albeit less ambitiously than the FIRA.

The Free Trade Agreement's (FTA) inclusion of a chapter on investment is a particularly interesting development. The chapter is clearly a product of compromise between two states with quite different views on investment regulation. The U.S. administration's view reflects the interests of a country that, until recently, has been a net-capital exporter. The Canadian government's view has been tempered by the ambivalence that Canadians show toward foreign investment (although it appears that concerns over policy autonomy are regionally based – mainly in central Canada – and most prevalent among the academic and cultural communities rather than shared by the population at large).[2]

This paper will examine the content and operation of Chapter 16 of the Free Trade Agreement. Before analyzing the chapter, however, I will place the issue in a broader context by describing some of the international instruments dealing with investment.

International Instruments Containing Investment Obligations

The central principle underlying the operation of the Investment Chapter is National Treatment. This principle has formed the basis for a number of bilateral and multilateral treaties and nonbinding instruments. As one of the original Contracting Parties to the General Agreement on Tariffs and Trade (GATT), Canada is no stranger to GATT's Article III which requires that National Treatment be extended with respect to trade in goods. Canada has also acceded to the 1961 OECD *Code of Liberalization of Capital Movements*, albeit with reservations, and has participated in the drafting of the 1976 OECD *Declaration on International Investment and Multinational Enterprises*. Both instruments contain National Treatment obligations.

The 1961 code – a legally binding instrument[3] adopted by the OECD council – states that countries should not employ regulations or practices including conditions or requirements affecting the operation of enterprises, that raise special barriers or limitations with respect to non-resident (as compared to resident) investors, and that have the intent or the effect of preventing or significantly impeding inward direct investment by non-residents. The code has a limited scope; it addresses transactions and transfers between residents and non-residents only. It does not impose obligations on the state regarding control of the investor after establishment.

The legal character is less clear than that of the code. The OECD convention contemplates "decisions" and "recommendations" by the council. No provision is made for "declarations". Thus, as Lévy notes, "[i]ts legal character is . . . determined by its wording and form, which give the measure of the extent to which the subscribing governments are expected to live up to such a declaration or to ensure that other addressees within their jurisdiction comply with them."[4] The collective view of OECD member states appear to regard the declaration as embodying "standards of behavior of a non-legal character" as significant moral, rather than legal obligations.[5]

The declaration exhorts OECD members to "accord to enterprises . . . owned or controlled directly or indirectly by nationals of another Member country . . . treatment under their laws, regulations and administrative practices, consistent with international law and no less favorable than that accorded in like situations to domestic enterprises."[6]

As would be expected, given the states' sensitivity to foreign direct investment, neither of the OECD instruments contain an unqualified National Treatment principle, either prior to or after establishment.

In addition to these instruments, multilateral negotiations are underway at the present time. One of the issues of greatest interest to the leading developed countries (Japan, the Community, and the United States) in the Uruguay Round of Multilateral Trade Negotiations (MTN) is the control of "trade-related investment measures" (TRIMs). The Punta del Este Declaration provides, "[f]ollowing an examination of the operation of GATT Articles related to the trade restrictive and distorting effects of investment measures, negotiations should elaborate, as appropriate, further provisions that may be necessary to avoid such adverse effects on trade."[7] Thus, it is likely that some form of GATT discipline on TRIMs will emerge from the Uruguay Round (probably in the form of an MTN Code *à la* the Tokyo Round).

Finally, there is a large body of bilateral investment treaties that provides evidence of state practice in this area. Gerhard Wegen notes that by 1985, Switzerland and the Federal Republic of Germany, for example, had entered into 30 and 53 such treaties, respectively.[8] The United States has also negotiated a number of investment treaties in the form of Friendship, Commerce and Navigation treaties and, more recently, Bilateral Investment Treaties.[9]

There is, therefore, a large body of international law and practice that forms the legal context in which the Investment Chapter can be viewed. While this paper does not purport to exhaustively compare the doctrinal and substantive aspects of Chapter 16 to other international instruments, it refers to bilateral and multilateral treaty practice by way of illustration.

Canada and International Investment Standards

Because of its role as a host state with significant foreign corporate presence in its economy, Canada has traditionally been wary of acceding to international investment obligations. It only recently became a signatory to the OECD *Code of Liberalization of Capital Movements* – and even then entered reservations with respect to, *inter alia*, right of establishment in order to protect its screening mechanism, Investment Canada. A party to the 1976 OECD declaration, Canada gained the distinction of becoming the first government to be challenged in the Committee on International Investment and

Multinational Enterprises (CIME), when a number of governments requested consultations regarding Canada's National Energy Policy.[10] Canada has not signed the *Convention on the Settlement of Investment Disputes between States and Nationals of Other States.*[11]

In light of this record, it is interesting to see an investment chapter in the Free Trade Agreement because its inclusion could be construed as a major shift in Canadian investment policy. One should be careful, however, to avoid exaggerating the chapter's significance. A review of the text reveals that it is not as dramatic a departure from Canadian practice as some observers and critics have alleged. On the contrary, the word "modest" comes to mind after closely perusing the chapter.

An Overview of Chapter 16

The overall scope and coverage of Chapter 16 is simply described:

1. The chapter does *not* apply to financial services (except for insurance), government procurement or transportation services.
2. The chapter establishes some basic rights and obligations (such as National Treatment, prohibition of certain performance requirements, safeguards in the event of expropriation). Importantly, these provisions do *not* apply to nonconforming provisions of existing measures. In other words, *all* existing discriminatory laws, practices, and policies in both Canada and the United States (and there are many!) are grandfathered under the Agreement.
3. Even where applicable, the National Treatment standard does not require identical treatment between domestic and foreign investments. Article 1602(8) permits differential treatment of foreign investors in defined circumstances:
    - so long as the difference is not greater than necessary for prudential, fiduciary, health and safety, or consumer protection reasons
    - the treatment is equivalent in effect to that accorded to domestic investors for such reasons
    - prior notification has been given to the other party.
4. The National Treatment obligation regarding the conduct and operation of business enterprises (Article 1602(1)(c)) does not apply to any measure affecting investments related to the provision of services other than services covered by the Agreement. Services *not* covered by Chapter 14 (Services) include transportation, basic telecommunications, medical, dental,

childcare, education and other social services. These, therefore, are not governed by Article 1602(1)(c).

5. Differential treatment in taxation and subsidy practices is permitted so long as this does not constitute a means of arbitrary or unjustifiable discrimination between domestic and foreign investors or a disguised restriction on the benefits accorded to investors under the chapter.
6. Investment Canada's ability to screen direct and indirect acquisitions (the United States does not have such a mechanism of general application) will be limited. The threshold for reviewing direct acquisitions by American firms will be raised from $5 million in gross assets to $150 million over four years. Indirect acquisitions will be phased out over the same period.

The cumulative effect of these provisions is that discriminatory investment controls cannot reasonably be said to be prohibited under the Agreement. On the contrary, while the Agreement moves toward more liberal treatment of capital movement, the grandfathering of all existing discriminatory measures, in and of itself, maintains very substantial discrimination in the investment regimes of both countries.

An Analysis of the Agreement's Obligations

Article 1602 sets out the basic principle of National Treatment. It provides as follows:

> Except as otherwise provided in this Chapter, each Party shall accord to investors of the other Party treatment no less favourable than that accorded in like circumstances to its investors with respect to its measures affecting:
>
> (a) the establishment of new business enterprises located in its territory;
>
> (b) the acquisition of business enterprises located in its territory;
>
> (c) the conduct and operation of business enterprises located in its territory; and
>
> (d) the sale of business enterprises located in its territory.

Chapter 16 is clearly intended to be one of the chapters that will bind subnational governments. National Treatment is further defined in Article 1602(4) to include provincial and state action:

> The treatment accorded by a Party under paragraph 1 shall mean, with respect to a province or a state, treatment no less favourable than the most favourable treatment accorded by such province or state in like circumstances to investors of the Party of which it forms a part.

The National Treatment principle should not be confused with reciprocity.[12] In trade in goods, for example, it does not require the importing state to regulate the sale of the subject goods in the same way that the exporting country does. Thus, for example, under the rule Canada can prohibit the importation of handguns because it prohibits their domestic sale as well. Similarly, with respect to investment, the rule does not require the host state to regulate an investment in the same way as the foreign investor's home state. The key point is that a state bound by the National Treatment rule may not discriminate between imported and domestically produced goods or, in the case of investment, discriminate between domestic and foreign investments.

It is important to note that the expression of the National Treatment principle begins with a qualification ("Except as otherwise provided for in this Chapter . . . "). Thus, National Treatment is not an absolute principle. The subsequent articles (Articles 1603-1606) prohibiting minimum equity requirements and forced divestitures, controlling the use of performance requirements, monitoring the power of expropriation and prohibiting restrictions on transfers of profits, royalties, fees, etc., are similarly qualified.

The qualification is found in Article 1607 (Existing Legislation) which states that the provisions of Articles 1602-1606 "shall not apply" to a nonconforming provision of any existing measure, the continuation or prompt renewal of a nonconforming provision of any existing measure, or an amendment to a nonconforming provision of any existing measure to the extent that the amendment does not decrease its conformity with any of the above-mentioned provisions.

The effect of Article 1607, therefore, is to freeze the existing state of discrimination in the signatories' economies. Thus, existing Canadian discriminatory measures with respect to ownership in the fields of broadcasting, energy and other parts of the Canadian economy are expressly permitted to continue, as are existing American measures that discriminate against Canadian investors.

An important point to note is that these discriminatory provisions cannot themselves be made more discriminatory. For example, if a particular piece of legislation were to restrict the level of foreign investment in a specific field without performance requirements, Article 1607 would not permit the legislation to be amended to impose discriminatory performance requirements. This is because the provisions of Articles 1602 to 1606 are expressly stated not to apply to a nonconforming *provision* of an existing measure, as opposed to the whole of an existing measure. Had the Agreement stated the latter, it would be open to take an existing discriminatory measure and change the actual means of discrimination within it. Article 1607 appears to prohibit this.

The effect of the interaction between Articles 1602 to 1606 and Article 1607, therefore, is to freeze the *status quo* insofar as discriminatory investment regulation is practised by the two countries. It warrants repeating that this does not preclude either signatory from legislating or regulating to achieve national objectives. The National Treatment obligation preserves the states' right to prescribe laws that are responsive to local or national conditions.

As noted above, having enunciated the basic principle of National Treatment, Chapter 16 then establishes specific obligations. These are as follows:

1. Article 1602(2): Neither party shall impose minimum equity requirements (other than nominal qualifying shares for directors or incorporators of corporations) on investors of the other.
2. Article 1602(3): Neither party shall require divestiture of an investment by an investor of the other party by reason of nationality.
3. Article 1603: Neither party shall impose performance requirements on an investor of the other as a term or condition of permitting an investment in its territory or in connection with the regulation of the conduct or operation of a business enterprise located in its territory. Not all performance requirements are prohibited. Only export requirements and domestic content requirements are proscribed.

   This provision is a compromise; the issue of performance requirements has been a long-standing matter of disagreement. In March 1982, a GATT panel was established to examine U.S. complaints over practices of the Foreign Investment Review Agency (FIRA). The panel found that undertakings required of foreign investors to purchase goods of Canadian origin or goods from Canadian importers were inconsistent with GATT's Article III National Treatment obligation.[13]

   Articles 1603 and 1604 incorporate the GATT ruling and go further to control export requirements (which the FIRA panel did not find inconsistent with GATT) as well as the potentially trade-distorting performance requirements imposed on investors of third countries. The articles do not control such performance requirements as R&D undertakings, technology transfers, world product mandates, etc. Yet, in the Uruguay Round, participants such as the European Community, Japan and the United States have signalled their interest in negotiating controls on these trade-related investment measures as well.

4. Article 1605: Neither party shall directly or indirectly nationalize or expropriate an investment in its territory by an investor of the other party or take measures tantamount to an expropriation, except in prescribed conditions: an expropriation must be for a public purpose; in accordance with due process of law; on a nondiscriminatory basis; and upon payment of prompt, adequate and effective compensation at fair market value.

   This is hardly controversial amongst the developed OECD states. While expropriation continues to be a divisive issue in relations between the Less Developed Countries and Developed Countries, the requirements of Article 1605 are generally viewed by the latter as recognized standards of international law.[13]

5. Article 1606: Neither party shall prevent an investor from transferring any profits from an investment including: dividends, any royalties, fees, interest and other earnings from an investment, or proceeds from the sale of all or any part of an investment or from the partial or complete liquidation of such an investment.

   A party, however, may prevent a transfer that is inconsistent with any measure of general application relating to such matters as bankruptcy, insolvency, creditors' rights, criminal or penal offences, withholding taxes, etc.

As noted above, these obligations are subject to the grandfathering provision of Article 1607.[14]

Chapter 16 permits four other forms of discrimination. Canada's general investment review law, the *Investment Canada Act*,[15] presently reviews acquisitions of Canadian businesses above $5 million in gross assets and indirect acquisitions of Canadian businesses above $50 million in gross assets. Review of direct acquisitions will continue to be permitted under the Agreement but the threshold for reviewing acquisitions will be raised substantially in four steps: To CAN$25 million in 1989; to CAN$50 million in 1990; to CAN$100 million in 1991; to CAN$150 million in 1992; and shall remain at CAN$150 million in constant third-anniversary-year dollars thereafter. Indirect acquisitions will be phased out by 1992.

Annex 1607.3, paragraph 2(a) indicates that Investment Canada's review will be to determine simply "whether or not to permit the acquisition." This is supported by the language of paragraph 3 of the same annex which provides that "[t]he guidelines or regulations pursuant to the *Investment Canada Act* shall be amended to provide that Canada shall comply with the provisions of paragraphs 2 and 3 of Article 1602 and the provisions of Article 1603." Thus, in the event that Investment Canada were to review an acquisition of a Canadian company with gross assets above $150 million in 1992, Investment Canada would not be permitted to impose requirements inconsistent with the Article 1602 National Treatment obligation or the Article 1603 prohibition against certain performance requirements. Thus, the review power is a bare power, with the exception of the oil, gas and uranium mining industries which are expressly exempted under paragraph 4 of Annex 1607.3.

Due to the prevalence of state-owned corporations in Canada at both levels of government, Article 1602 contains three paragraphs which address the aspects of privatization of Crown corporations. In essence, Canada may introduce any new measure in relation to a Crown corporation that is carried on at the date of entry into force of the Agreement that is inconsistent with the National Treatment and minimum equity rules and relates to the acquisition and sale of such a business enterprise or relates to its direct or indirect ownership. Once it has done so, however, it shall not make the measure *more* inconsistent with the National Treatment and minimum equity rules. In short, the Agreement allows for Canadian privatization of Crown corporations through share offerings restricted to Canadian citizens.

Further, discrimination is expressly provided for in the areas of taxation and subsidy practices. Article 1609 grants a qualified right to employ discriminatory taxation or subsidy practices. Both are subject to Article 2011 (Nullification and Impairment). According to paragraph 1 of Article 1609, subject to the nullification and impairment provision, "this Chapter shall not apply to any new taxation measure, provided that such measure does not constitute a means of arbitrary or unjustifiable discrimination between investors of the Parties or a disguised restriction on the benefits accorded to the investors of the Parties under this Chapter." Paragraph 2 (Subsidies) also incorporates the "arbitrary or unjustifiable discrimination or a disguised restriction" qualifications. Clearly, this article could be the subject of dispute between the two parties, recognizing as it does the right to discriminate but, at the same time, qualifying that right by reference to the standards of "arbitrary or unjustifiable discrimination and disguised restriction" and expressly subjecting it to the general nullification and impairment provision.

Dispute Settlement

Chapter 16 contains a special provision on investment disputes. It is noteworthy that any determination made by Canada pursuant to the *Investment Canada Act* whether to permit a reviewable acquisition, is exempted from the Agreement's dispute settlement provisions. In addition, each party and their investors retain their respective rights and obligations under customary international law with respect to portfolio and direct investment not covered under the chapter or to which its provisions do not apply. In the case of investments not covered by Chapter 16, therefore, disputes could be dealt with under the rules of customary international law or in other international fora.

Article 1608 stands in rather stark contrast to conventional international law and U.S. bilateral treaty practice. The sharp attitudinal differences between Canada and the United States are most evident in the article on dispute settlement. Whereas the United States has been a signatory and strong supporter of the International Centre for the Settlement of Investment Disputes (ICSID) and has sought the inclusion of compulsory arbitration provisions in its Bilateral Investment Treaties, Canada has evidenced a very different attitude; Canada has not acceded to the ICSID convention because of the required submission to compulsory arbitration.

The sharp difference in views between a capital importer and a capital exporter (recently turned importer) is reflected in Article 1608; the United States did not achieve its negotiating goal of compulsory arbitration of investment disputes. Indeed, there is no reference to the ICSID convention as the primary international treaty dealing with the settlement of such disputes. The compromise is a kind of "best efforts" clause; paragraph 4 provides that where the Agreement's institutional provisions are invoked to resolve an investment dispute, "the Parties and the Commission shall give the fullest consideration, in any particular case, to settling any dispute regarding the interpretation or application of this Chapter by arbitration or panel procedures." Clearly, this hortative language does not impose an obligation to send disputes to binding arbitration.

Recognizing the special nature of investment disputes, however, the parties did agree that they "shall make every attempt to ensure that the panelists are individuals experienced and competent in the field of international investment." In addition, a panel "shall take into consideration how such disputes before it are normally dealt with by internationally recognized rules for commercial arbitration." This open-textured language would permit panelists to take into consideration the rules and procedures of ICSID, the practice of International Chamber of Commerce (ICC) arbitrations (7 per cent of which deal with investment disputes between a state and the national of another state), and other international arbitral bodies.

A Brief Comparison of the Provisions of the Free Trade Agreement with the Model Bilateral Investment Treaty

In 1981, the United States started the Bilateral Investment Treaty program under which it negotiated a series of treaties with a number of other countries. The Bilateral Investment Treaties (BITs) deal with essentially four major issues:

- nondiscrimination with respect to the establishment and operation of an investment in each signatory
- the right to transfer abroad capital and profits from the signatory
- protection against expropriation
- mandatory dispute settlement for disputes between foreign investors and the host government or between the two parties.

A comparison between the model BIT and Chapter 16 of the FTA reveals substantial differences. First, whereas investment is defined narrowly under the FTA to deal essentially with the establishment, acquisition or operation of an existing or new business enterprise, Article l(c) of the model BIT defines investment to include intangible property, claims to money (or a claim to performance having economic value), intellectual property rights, industrial property rights, licences, permits and other rights conferred by contract. This definition is far broader than the definition found in Article 1611 of the FTA.

Article 2 of the model BIT contains an elaborate enunciation of the National Treatment principle, including matters such as the making, performance and enforcement of contracts; the acquisition, ownership and disposal of personal property both tangible and intangible; the acquisition, maintenance and protection of copyrights, patents, etc.; the borrowing of funds; and the purchase and issuance of equity shares. Article 1602 of the FTA, on the other hand, restricts the operation of National Treatment to the establishment of new business enterprises, their acquisition, conduct, operation and sale.

The model BIT also includes a "fair and equitable treatment" standard to protect foreign investors against host government action. The FTA does not contain such a standard. Article 2, paragraph 6 of the model BIT requires conditions of competitive equality where government-owned corporations or instrumentalities compete with private parties. The FTA does not contain such a provision. Article 2, paragraph 7 of the model BIT prohibits performance requirements such as export and domestic content rules. The FTA's Article 1603 contains similar prohibitions.

Article 3 of the model BIT sets out the grounds for compensation for the expropriation of an investment. Article 1605 of the FTA substantially tracks the language of Article 3. The only difference between the two otherwise similar provisions is that the FTA does not include the BIT's specific reference to the requirement that an expropriation not "violate any specific provision on contractual stability or expropriation contained in an investment agreement" between the investor and the host government. In addition, the FTA does not contain the kind of definition and detail that is found in the BIT regarding terms such as "fair market value" when determining compensation.

As noted earlier, one of the major issues of disagreement between the parties is that of dispute settlement. For example, Article 3, paragraph 3 of the BIT grants to a foreign investor the right of access to the judicial or administrative authorities of the party alleged to be expropriating its investment. This is to determine whether or not an expropriation has indeed occurred and if so, whether it and any compensation therefor conforms to the principles of international law expressed in the article. There is no equivalent provision in the FTA.

Perhaps most significantly, whereas Article 7 of the model BIT expressly refers to ICSID and requires compulsory arbitration of disputes between an investor and the host government, or between the parties to the agreement, there is no such provision in the FTA.

Conclusion

Chapter 16 contains some disciplines in relation to Canada's investment regulation policy. But the extent to which these disciplines "infringe" Canadian freedom of action should not be exaggerated. Since the National Treatment rule underlies the chapter's operation, little in the chapter can be said to infringe Canada's ability to legislate or regulate in order to achieve Canadian objectives—except that Canada cannot discriminate between Canadian and American investment in ways that are not permitted under the Agreement.

Canada has 40 years of experience with the National Treatment rule respecting trade in goods. During that time, Canada has been able to pursue significantly different regulatory policies than those of the United States. For example, Canada has legislated against the production and distribution of hard-core pornography, has required bilingual labelling of goods, and has prohibited the importation and sale of handguns. These policies have been in furtherance of public morals, language, culture, and objectives of law and order. These are permitted by the National Treatment rule because they do not attempt to discriminate between foreign and domestic goods.

The National Treatment rule has largely insinuated itself into the fabric of Canadian trade regulation. While in international legal terms, National Treatment is a profoundly important principle, it has largely been ignored by Canadians. This is because National Treatment is a sovereignty-respecting principle. The principle makes no attempt to define national objectives; it merely regulates the means of achieving them.

With the extension of the National Treatment principle to the field of investment – albeit with major qualifications – Canada is unquestionably taking a step toward liberalization of capital movement. No doubt investment disputes will arise between the two countries. There is language in Chapter 16 that cries out for legal argument and further elaboration by binational panels. Nevertheless, a textual analysis of Chapter 16 suggests that the step forward is a modest one.

Notes

1. S.C. 1973-74, c. 46, as am. S.C. 1976-77, c. 52.

2. For a discussion of views on foreign direct investment in Canada, see J.A. Finlayson, "Canadian International Economic Policy: Context, Issues and a Review of Some Recent Literature" in D. Stairs & G.R. Winham eds, *Canada and the International Political Economic Environment* (Toronto: University of Toronto Press, 1985) 9 at 69-72.

3. P. Lévy, "The OECD Declaration on International Investment and Multinational Enterprises" in S.J. Rubin & G.C. Hufbauer eds, *Emerging Standards of International Trade and Investment* (Totowa, N.J.: Rowman & Allanheld, 1984) 47 at 48.

4. *Ibid.* at 49.

5. *Ibid.* at 50.

6. *Ibid.* at 54.

7. See *Basic Instruments and Selected Documents* (1985-86), GATT (33d Supp.) at 26.

8. Gerhard Wegen, "Dispute Settlement and Arbitration" in S.J. Rubin & R.W. Nelson eds, *International Investment Disputes: Avoidance and Settlement* 59 at 66.

9. See Pamela B. Gain, "The U.S. Bilateral Investment Treaty Program" (1985) 21 Stan. J. Int'l L. 373.

10. *Lévy, supra,* note 3 at 56.

11. (1965) 4 I.L.M. 524.

12. See in this regard, M.M. Hart, "The Mercantilist's Lament: National Treatment and Modern Trade Negotiations" (1987) J.W.T.L. 37.

13. See GATT Activities (1983) at 39-41.

14. It should be noted that the term "existing measure" has an additional meaning for the purposes of Chapter 16. In Chapter 2, the definition of measure "includes any law, regulation, procedure, requirement or practice." Article 1611 provides that "measure shall have the same meaning as in Article 201, except that it shall also include any published policy."

15. 33 & 34 Eliz. 2, c. 20, 1984-85.

Energy and the National Treatment Rules vs. Discriminatory Policies

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Rowland J. Harrison

Introduction

The October 1987 Elements of Agreement for a Canada-U.S. Free Trade Agreement (the FTA) stated with respect to energy, that the two nations had reached "broad agreement to assure the freest possible bilateral trade in energy, including nondiscriminatory access for the United States to Canadian energy supplies and secure market access for Canadian energy exports to the United States."[1] It is clear from the text of the final Agreement, however, that this objective is by no means synonymous with complete deregulation of energy trade between the two nations, nor with the absence of all discriminatory policies.

This paper discusses those aspects of the FTA that contemplate some form of discriminatory policies by Canada with respect to either the export of energy goods from Canada to the United States, or investment by U.S. nationals in the Canadian energy industry. More specifically, the paper reviews the FTA's provisions with respect to export restrictions, incentives for oil and gas exploration and development, investment in the oil and gas sector and finally, the supply of Canadian goods and services and the employment of Canadians in oil and gas developments.

The October Elements of Agreement raised as many questions as they answered with respect to the proposed treatment of energy trade.

Many of these are answered by the final Agreement, but it cannot be said that the Agreement itself is a model of clarity in all respects. Indeed, within days of its signing on January 2, 1988, opposing views were being expressed with respect to whether it would prevent the United States from imposing restrictions on imports of Canadian oil and petroleum products in the interests of national security.[2]

The significance of this in the present context is that it signals the potential for ongoing disagreements arising from the interpretation of the Agreement. This potential becomes greater still when it is considered that the Agreement has not been universally welcomed by all participants in the U.S. energy sector. The president of the Texas Independent Producers and Royalty Owners Association, for example, has been quoted as stating that the Agreement carries "a hidden threat to the energy security of the U.S."[3] The Independent Petroleum Association of America is also on record as being opposed to Congressional ratification of the Agreement "unless all current U.S. and Canadian regulatory practices which give Canadian natural gas preferential treatment in U.S. markets are eliminated . . . ."[4]

The existence of such reservations with respect to the merits of the FTA means that any ambiguity in its provisions will inevitably be exploited to the fullest extent. This means, in turn, that the precise provisions of the implementation of the FTA will become critical to any assessment of what it has really accomplished. Analysis of the text of the Agreement at this time can only give an incomplete picture, although such analysis is, of course, a necessary starting point.

The FTA clearly contemplates some form of ongoing regulation of energy trade. Indeed, several features make it clear that the existing legislative and regulatory framework for energy exports from Canada will be maintained, except as otherwise specified in the Agreement. The real impact of the Agreement will be determined, therefore, by the actual implementation of specific measures required as departures from the *status quo* and, perhaps more importantly, by the extent to which future regulatory decisions, within the existing legislative framework, are constrained.

Export Restrictions

The energy provisions of the Free Trade Agreement are directly linked to the relevant provisions of the General Agreement on Tariffs and Trade (GATT), with the parties affirming their respective rights and obligations thereunder with respect to prohibitions or restrictions on bilateral trade in energy goods.[5] A number of specific provisions then follow.

First, by Article 902.2 the parties acknowledge that their GATT rights and obligations prohibit minimum export price requirements "in any circumstances in which any other form of quantitative restriction is prohibited" by the GATT. This appears to be a reference principally to Article XI.1 of the GATT which generally prohibits the institution or maintenance of restrictions on the exportation or sale for export of any product, subject to certain exceptions. The result is that the FTA generally prohibits minimum export price requirements for energy goods.

Article 903 of the FTA then prohibits the maintenance or introduction of any tax, duty or charge on the export of any energy good to the other party, "unless such tax, duty, or charge is also maintained or introduced on such energy good when destined for domestic consumption." This provision clearly prohibits an export tax as such.

Article 904 deals with export restrictions in the context of a reduction in the supply of an energy good. It has four component parts. First, any restriction must be "otherwise justified under the provisions of Articles XI:2(a) and XX(g), (i) and (j) of the GATT with respect to the export of an energy good of the Party to the territory of the other Party . . . ." The first of these articles of the GATT provides an exception to the general elimination of quantitative restrictions, in the case of an export prohibition or restriction "temporarily applied to prevent or relieve critical shortages of foodstuffs or other products essential to the exporting contracting party . . . ." This threshold must be crossed before reaching the provisions of Article 904 of the FTA. Alternatively, Canada would have to cross one of the thresholds for the adoption of restrictive measures under the specified paragraphs of Article XX of the GATT. The most relevant of these will likely prove to be paragraph (g) which permits measures "relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption . . . ."

Under Article 904, if a Canadian restriction were justified under any of these provisions of the GATT, it would then be subject to three further limitations. The first of these is the proportionality requirement, providing that the restriction could not reduce the proportion of the total export shipments of a specific energy good "made available to" the other party, relative to the total supply of that good by Canada as compared to the proportion prevailing during a preceding 36-month period. Secondly, Canada could not impose a higher price for exports by means of measures such as licences, fees, taxation and minimum price requirements, although this provision is stated to not apply to a higher price resulting from a restriction on the volume of exports. Thirdly, the restriction must not require the disruption of normal channels of supply or normal proportions among specific energy goods "such as, for example, between crude oil and refined products and among different categories of crude oil and of refined products."

"Total supply" for the purposes of this article is defined by Article 909 to mean: ". . . shipments to domestic users and foreign users from (a) domestic production, (b) domestic inventory, and (c) other imports, as appropriate." This leaves the details of the proportionality requirement somewhat vague, although this appears to have been the intention of the parties. In an explanatory document released within a matter of days of the FTA,[6] the Department of Energy Mines and Resources (EMR) gives examples of situations in which different means of measuring total supply for the purposes of the proportionality requirement would be appropriate. For example, if a reduction in supply resulted entirely from a reduction in domestic Canadian production, the department argues that a narrow definition of total supply, to exclude imports, would be appropriate. If, however, a shortage resulted from a decline in Canada's imports of crude oil, the proportionality calculation should be based on a broader definition of total supply to include imports.

The potential for dispute seems to be clear, both as to the calculation of the proportions protected by Article 902 and with respect to the methods of implementing any authorized restrictions. The EMR document states:[7]

> The actual method of implementing proportionality would be determined by the government of the day. Proportional restrictions could be imposed by declining to authorize new export licences, limiting the extension of existing licences, or reducing the quantities authorized under existing licences. Due account could be taken of contractual relationships and channels of supply that might exist at the time that restrictions were under consideration.

These words offer little reassurance as to just what the implications of Article 904 are. The document does, however, emphasize what appears to be clear from the FTA itself with respect to the nature of Canada's obligations in the event of supply disruptions. That obligation is to refrain from imposing restrictions that are not within those authorized by the exceptions in the FTA. There is not, in other words, any obligation imposed actually to supply energy goods to the levels resulting from the application of the proportionality calculation provided for in Article 904. Rather, the result is that the U.S. buyers of Canadian energy goods are guaranteed access to that proportion on commercial terms. Canadians would not be precluded or prevented from competing for the same energy goods on commercial terms.

The final provision of the FTA dealing specifically with export restrictions provides for national security measures where necessary to supply a military establishment or to enable fulfillment of a critical defense contract, to respond to an armed conflict, to implement policies relating to the nonproliferation of nuclear weapons or to respond to direct threats of disruption in the supply of nuclear materials for defense purposes.[8] Again, these measures are subject to meeting the threshold requirements of Article XXI of the GATT (Security Exceptions) or Article 2003 of the FTA (National Security).

As indicated above, the principal source of difficulty in determining the real impact of the energy chapter of the FTA lies not so much in these specific provisions as it does in the domain that is left to Canada for regulating exports of energy goods. Discussion of this question begins with Article 905, which provides:

> If either Party considers that energy regulatory actions by the other Party would directly result in discrimination against its energy goods or its persons inconsistent with the principles of this Agreement, that Party may initiate direct consultations with the other Party.

This provision serves two purposes so far as the present discussion is concerned. Firstly, it acknowledges that each party will continue "energy regulatory actions," thus making it clear that there will continue to be regulation of trade in energy goods between the parties. Secondly, it explicitly acknowledges that such actions may result in discrimination against energy goods originating with the other party and that such actions may be inconsistent with the principles of the FTA.

The article goes on to specify that an "energy regulatory action" shall include actions by, *inter alia*, the National Energy Board (NEB) in Canada, and the Federal Energy Regulatory Commission (FERC) or the Economic Regulatory Administration in the United States.

This article also requires Canada to eliminate the " least cost alternative test" provided for in subparagraph 6(2)(z)(iii) of the *National Energy Board Part VI Regulations*, with respect to the authorization of electricity exports. It is clearly contemplated, however, that the other tests specified under subparagraph 6(2)(z) (namely, recovery of Canadian costs and that the export price would not be less than the price to Canadians for equivalent service in related areas) will continue to be required.

Paragraph 4 of Annex 905.2 is also significant. It provides:

> It is understood that the implementation of this Chapter includes the *administration* of any "surplus tests" on the export of any energy good to the other Party in a manner consistent with the provisions of Articles 902, 903 and 904. (Emphasis added.)

The Synopsis accompanying the release of the Free Trade Agreement states that both Canada and the United States "remain free to determine whether and when to allow exports and may continue to monitor and license exports."[9]

It appears from these provisions that, in one sense, the National Energy Board will continue to exercise much of the jurisdiction that it presently has. It does not seem to be contemplated, for example, that section 83 of the *National Energy Board Act*,[10] requiring a determination that energy exports are surplus to Canada's reasonably forseeable requirements, will be repealed.

At the present time, however, NEB policies or regulations are such that there would not appear to be any inconsistency with the FTA, either as to the licensing of exportable quantities of electricity, oil or natural gas or with respect to export pricing of those energy goods. Short-term exports of oil from Canada have not been constrained as to price or volume since June 1, 1985. In the case of natural gas, there is no longer any requirement for the prior approval of export prices. Rather, prices are monitored by a committee of federal and provincial officials to advise the respective energy ministers about the relationship between domestic and export gas prices. Gas exports were further deregulated with the NEB's decision in July 1987 to abandon its requirement that only gas that is surplus to a volume determined by a reserves-to-production ratio could be licensed for export as being surplus to Canada's reasonably forseeable requirements. Instead, the Board adopted a new "market-based procedure" for satisfying itself that exports of Canadian gas were surplus.[11]

In the past, however, the NEB has exercised its section 83 jurisdiction to severely constrain the export of natural gas above levels calculated by the application of rigid mathematical formulae. A return to such applications of section 83 would clearly be contrary to the FTA.

It is equally clear from Article 905 and Annex 905.2 that the FTA will not directly resolve regulatory problems in Canada-U.S. energy trade. The ongoing role of the National Energy Board in Canada, as well as the Federal Energy Regulatory Commission and the Economic Regulatory Administration in the United States, is acknowledged in Article 905.1 of the FTA. Indeed, the EMR explanatory document referred to earlier notes that the provision "does not eliminate existing regulations, such as the FERC 'as billed' decision for natural gas."[12] The document states that the right to initiate consultation provides a means to formalize existing *ad hoc* attempts to deal with regulatory problems. Again, the real impact of the FTA will be determined by actions taken pursuant to this consultation mechanism.

Resource Development

Article 906 of the FTA provides that the parties have agreed "to allow existing or future incentives for oil and gas exploration, development and related activities in order to maintain the reserve base for these energy resources." Conceivably, future disputes could arise under this provision with respect to the question of whether a particular incentive constitutes a subsidy. In the shorter term, the provision may allow for a form of *de facto* discrimination, inasmuch as the projects that will attract such incentives will more likely be Canadian-sponsored developments,[13] or projects in frontier areas that are subject to the 50 per cent Canadian ownership requirement imposed by the *Canada Petroleum Resources Act*.[14]

Investment

Article 1607 of the FTA provides that existing measures with respect to investment can be maintained. This means with respect to the oil and gas sector firstly, that the existing policy under the *Investment Canada Act*[15] with respect to the takeover of Canadian energy firms will be maintained. The policy is as follows:[16]

- foreign interests can commence operations in Canada to explore for oil and gas without restrictions;
- foreign acquisitions of control of Canadian-controlled firms, with gross assets of $5 million or more, will be rejected if the company is in good financial health;
- if the company is unhealthy, the proposal will be permissible, if it is of positive net benefit, subject to satisfactory corporate undertakings on equity, investment and employment;
- foreign acquisitions of control of already foreign controlled firms, with gross assets of $5 million or over, will generally be permitted, subject to satisfactory undertakings regarding Canadian participation and exploration spending (in the case of direct acquisitions of control the threshold for review is $5 million of gross assets when more than 50 per cent of the

assets are located in Canada; otherwise the threshold is $50 million); and

- there is a 50 per cent Canadian ownership requirement for issuance of a production licence on Frontier Lands.

Secondly, the Canadian ownership requirements of the *Canada Petroleum Resources Act*[17] will be maintained. These are frequently stated to require 50 per cent Canadian ownership for production licences for projects on Canada's frontier lands, off the east and west coasts and in the north. In fact, however, the requirements of that act are much less onerous. In effect, they provide that the proponents of a development project must file with the minister a Canadian ownership plan outlining the means by which the proponents expect to take the ownership of the project to 50 per cent before production commences. If the 50 per cent level is not in fact attained by that point, the minister may waive the requirement or, alternatively, may require the proponents to offer for sale by public auction a portion of the project sufficient to bring the Canadian ownership level to 50 per cent. In the event that a sale does not result from this auction, the government itself has an option to acquire this share, failing which the project proceeds, notwithstanding that its Canadian ownership level is below 50 per cent. In other words, the requirements simply amount to providing an opportunity for Canadians to acquire ownership of a project up to a level of 50 per cent on commercial terms. When understood in these terms, it is perhaps not surprising that the Canadian ownership requirements of the *Canada Petroleum Resources Act* were grandfathered by the FTA.

The *Canada Petroleum Resources Act* also provides that no share in a production licence can be transferred without ministerial approval.[18] In order to determine whether to approve a proposed transfer, the minister may take into account the impact of the transfer on the Canadian ownership rate of the licence.[19] The implication is that a transfer that would lower the Canadian ownership rate would likely not be approved. The purpose is, of course, to provide a mechanism to protect the Canadian ownership rate of a production licence when first issued.

The EMR explanatory document also notes that the grandfathering provisions of the Investment Chapter of the FTA also apply to "Canada's policy objective of 50 per cent Canadian ownership of upstream oil and gas revenues . . . ."[20] The impact of this provision is likely to be minimal, however, as the policy is nothing more than that there is no mandatory requirement for minimum Canadian ownership levels of upstream oil and gas revenues other than those applicable to production licences for developments on Canada's frontier lands, the impact of which will not be felt until major projects are developed in the frontier areas.

Canada Benefits

The final aspect of the FTA which contemplates some form of discrimination in energy regulation relates to requirements with respect to the supply of Canadian goods and services and the employment of Canadians in oil and gas projects on Canada's frontier lands. The relevant legislation requires ministerial approval of a "plan for the employment of Canadians and for providing Canadian manufacturers, consultants, contractors and service companies with a full and fair opportunity to participate on a competitive basis in the supply of goods and services used in any proposed work or activity . . . ."[21] The minister may also require that such plans "include provisions to ensure that disadvantaged individuals or groups have access to training and employment opportunities and to enable such individuals or groups or corporations owned or cooperatives operated by them to participate in the supply of goods and services used in any proposed work or activity . . . ."[22] The legislation implementing the Newfoundland and Nova Scotia Accords contains similar provisions with respect to residents of those provinces and the supply of goods and services from those provinces.[23] These provisions are not affected by the FTA.

Conclusion

With some specific exceptions, the energy provisions of the Canada-U.S. Free Trade Agreement are largely intended to maintain the *status quo* with respect to the regulation of energy trade between the two nations. This includes maintaining the regulatory framework and institutions that each of the parties presently has in place.

Over the past few years, both Canada and the United States have been moving toward the deregulation of energy trade. Thus, a commitment to "the freest possible bilateral trade in energy" between the two nations is consistent with – indeed, an inevitable consequence of – existing national policies. The significance of the FTA with respect to energy is found, therefore, not so much in its present impact, but rather in the extent to which it will constrain future government actions.

It is to be emphasized in this regard that in both countries the process of so-called "deregulation" has really been a process of "re-regulation." That is to say, the broad regulatory framework with respect to energy trade has been maintained, but the policies developed and implemented within that framework have been more consistent with the free market movement of energy goods. While the regulatory framework remains in place, however, there will continue to be a potential for "regulatory actions" (in the words of the FTA itself) that will impede free trade in energy goods between the two nations. It is likely, therefore, that the FTA has not succeeded in removing all impediments to the totally free movement of energy goods between the two nations and that there will continue to be complications. As these develop, inevitably the respective parties will advance differing interpretations of the FTA to support their positions. The FTA has, however, at least articulated a common objective. Disputes are, therefore, more likely to be confined to the specifics of individual cases or actions.

Notes

1. Preliminary Transcript, *Canada-United States Free Trade Agreement*, "Elements of the Agreement" (1987) at 16.
2. See *The (Toronto) Globe and Mail*, (5 January 1988) 4.
3. Statement by John Watson, President of the Texas Independent Producers and Royalty Owners Association, reprinted in (November 1987) *Offshore* at 6.
4. Statement by the Independent Petroleum Association of America, reprinted in (26 October 1987) *Oilweek* at 7.
5. *Canada-United States Free Trade Agreement* (19 December 1987) art. 902.1 [hereinafter FTA].
6. Energy, Mines and Resources Canada, "The Canada/United States Free Trade Agreement: What It Means to You" (January 1988).
7. *Ibid.* at 10. The statement is repeated in a later, more formal document published by Energy, Mines and Resoures Canada, entitled "The Canada-U.S. Free Trade Agreement and Energy: An Assessment."
8. FTA, art. 907.
9. *Canada-United States Free Trade Agreement*, "Synopsis" (10 December 1987) at 30.
10. *National Energy Board Act*, R.S.C. 1970, c. N-6.

11. See National Energy Board, *Reasons for Decision: In the Matter of Review of Natural Gas Surplus Determination Procedures* (July 1987).

12. *Supra*, note 6.

13. Interestingly, the EMR explanatory document stated that Canada could continue "to use policies and programs such as case-by-case support for oil and gas megaprojects."

14. *Canada Petroleum Resources Act*, S.C. 1986, c. 45. Discussed further, *infra*, note 17.

15. *Investment Canada Act*, S.C. 1985, c. 20.

16. As stated in Energy, Mines and Resources Canada, "The Canada-U.S. Free Trade Agreement and Energy: An Assessment" (1988) at 34.

17. *Canada Petroleum Resources Act*, S.C. 1986, c. 45, Part V.

18. *Ibid.* at s. 86.

19. *Ibid.* at s. 86(2), para. 11.

20. *Supra*, note 6.

21. See *Oil and Gas Production and Conservation Act*, R.S.C. 1970, c. 0-4, s. 3.4(1) (as am.).

22. *Ibid.* s. 3.4(3).

23. In Newfoundland, see the *Canada-Newfoundland Atlantic Accord Implementation Act*, S.C. 1987, c. 3, s. 45. At the time of writing, implementation of the *Canada-Nova Scotia Accord* is before Parliament in Bill C-75, for the *Canada-Nova Scotia Offshore Petroleum Resources Accord Implementation Act*. See s. 45.

VII.

The Constitutional Dimensions

Implementing the Canada-United States Free Trade Agreement

H. Scott Fairley

Introduction

The Canada-United States Free Trade Agreement (FTA),[1] signed by Prime Minister Mulroney and President Reagan on January 2, 1988, now faces a rocky road to implementation and ratification on both sides of the border. In the United States, there is no constitutional uncertainty as to the power of Congress to enact the implementing statute; the only question is whether the politics between the White House and Capitol Hill will prompt Congress to do what the President requests. On that score, a constitutional separation of powers between President and Congress precludes any guarantees.[2] For Canada, the shell game is markedly different but no less hazardous. In fact, it is probably more so in view of the potential involvement of a greater number of governmental actors.

Here, there is little doubt that ultimately, Parliament will do the bidding of the Mulroney government. A majority of seats commanding the will of the House of Commons provides most if not all the assurance Mr. Mulroney needs, notwithstanding the possibility of obstruction from a Senate currently dominated by a hostile political party.[3]

Rather, our uncertainty arises from limitations on the constitutional jurisdiction of Parliament to enact all the legislation the government of Canada requires to implement the deal. This is a "division of powers" question under the Constitution of Canada as between the mutually exclusive jurisdiction of Parliament and the provincial legislatures.[4] To the extent that the legislative "subject matter" of the FTA may be said to lie within provincial jurisdiction, conventional constitutional wisdom dictates that Parliament has no additional legislative jurisdiction simply by virtue of making a commitment to a foreign sovereign. This is the rule, so-called, of the celebrated (or infamous) *Labour Conventions* case of 1937.[5] In the result, provincial governments who withhold their agreement to enact complementary legislation can undercut federal foreign policy initiatives.

Assuming existing conventional wisdom remains undisturbed, the problem is to determine the scope of jurisdiction each level of government wields with respect to the contents of the FTA. This becomes a key issue only because three Canadian provinces have registered their opposition to the Agreement as a whole – Manitoba, Ontario and Prince Edward Island. Had all the provinces agreed, the processes of cooperative federalism[6] would have been sufficient to carry the day; but once again, these have fallen short.[7] Thus, the particularly vociferous opposition from Ontario – the most populous and economically powerful province in Canada – to perhaps the most ambitious federal treaty initiative of the century, smacks of a possibly far-reaching constitutional confrontation.

With the foregoing to set the stage, I proceed with a brief treatment of existing constitutional doctrine which the implementation controversy should suggest is a major Canadian constitutional disability in need of redress. I then turn to the contents of the FTA in relation to competing federal and provincial claims of jurisdiction. The next section of the paper deals with potential constitutional arguments for and against comprehensive federal implementing legislation in the event of a provincial legal challenge or on the assumption that a constitutional reference is forthcoming from either level of government. I conclude by leaving the reader with a few tentative observations on alternative *denouements*.

Part I

The major point of the *Labour Conventions* case was that the acquisition of external obligations by Canada had no constitutional impact on the federal division of powers demarcated in the *British North America Act, 1867*, now the *Constitution Act, 1867*.[8] It stood notwithstanding the recent acquisition of international personality by the national government[9] which had been formally recognized after the fact by the *Statute of Westminister, 1931*.[10] Section 132 of the act of 1867, which gave a colonial Parliament plenary jurisdiction to implement "Empire treaties," not the homegrown variety, did not survive Canada's transition from colonial to international status. We learned that organic constitutions received little fertilizer from the Privy Council;[11] and, given the Law Lords' interpretation of the Canadian federal state in its colonial context, there was no room left over for admitting a new candidate to the ranks.[12]

Thus, Lord Atkin concluded in the single if not unanimous opinion[13] of the Judicial Committee:

> For the purposes of ss. 91 and 92, i.e., the distribution of legislative powers between the Dominion and the Provinces, there is no such thing as treaty legislation as such. The distribution is based on classes of subjects; and as a treaty deals with a particular class of subjects so will the legislative power of performing it be ascertained.[14]

Lord Atkin reasoned further that, "[w]hile the ship of state sails on larger ventures and into foreign waters she still retains the watertight compartments which are an essential part of her original structure."[15] Adherence to an internalized perspective premised on similarly based principles of exclusivity and exhaustiveness allowed that "foreign waters" could be ignored in defining domestic constitutional limitations. The Constitution of Canada was no longer a purely domestic affair. But no matter, "[i]n totality of legislative powers" Canada was "fully equipped" so that any legislative scheme could be effected "by co-operation between the Dominion and the Provinces."[16]

The *Labour Conventions* case has always been something of a whipping boy, at least in Anglo-Canadian legal scholarship.[17] But it also has a principled justification in which its apparent vindication of the "federal principle,"[18] which has made it the darling of classical federalists,[19] not to mention a well-understood rallying point for provincial premiers who want to thwart federal foreign policy initiatives. I believe, however, that there is a more, or at least equally competitive argument on the other side.

What *Labour Conventions* lacks, and what continues to elude precise articulation in any Canadian constitutional authority to date, lies in an appreciation of international legal personality and sovereignty as a constitutional foundation for national authority, independent of specific constitutional language. Under such a view, federal power over external affairs is inherent in the nature of the Canadian nation-state and serves as an additional constitutional basis for resolving federalism controversies where the international status and responsibilities of Canada to foreign governments are implicated.[20] Such would be the case if, for example, the Province of

Ontario chose to apply its existing laws or enacted subsequent laws inconsistent with federal implementation of the FTA.

The possible contours of such an argument have been hinted at by the Supreme Court of Canada for quite some time.[21] But the deficiency is really broader and more fundamental than the traditional doctrinal rubric of treaty implementation suggests. Rather, Canada has been long in need of a constitutionally recognized, comprehensive and reviewable federal external affairs power. In my view, this new jurisdiction can be judicially derived within the confines of the federal general power in the existing Constitution,[22] subject to judicial review in the manner of other federal division of powers questions when Ottawa is seen to encroach on provincial domains. Indeed, there are compelling principled as well as practical reasons for the courts to facilitate a process which, it bears emphasis for the benefit of both classical federalists and provincial sensibilities, need not constitute a simplistic overruling of the *Labour Conventions* case. Nevertheless, it would refute Lord Atkin's conclusion that "there is no such thing as treaty legislation as such."[23]

The details of the foregoing argument[24] go well beyond my purpose here, except to suggest that federal-provincial controversy over the FTA could become a catalyst for constitutional revision by the courts or, contrariwise, a potentially (but not necessarily) embarrassing reaffirmation of the *status quo*. Either way, the issue deserves great care, not to mention a serious rethinking of conventional wisdom by both federal and provincial actors. That said, it remains to discover, even if *Labour Conventions* governs the day, where the decisive balance of legislative power lies.

Part II

The position of the Mulroney government, in rather imprecise terms, has been that virtually all of the FTA comprises matters amenable to federal jurisdiction.[25] On the provincial side, a very different perspective is offered by the Attorney General of Ontario whose December 15, 1987 address to the Canadian Bar Association in Toronto asserted that the FTA was nothing less than a jackbooted federal invasion of provincial rights.[26] Clearly, someone is mistaken.

Where the greater margin of error lies depends on a good deal less than absolutely clear judicial signals in Canadian federalism jurisprudence, in particular with respect to the critical field of federal Trade and Commerce jurisdiction. After all, it is a trade agreement which Canada and the United States have signed. Nevertheless, for many Canadians, the FTA connotes much more and it is the penumbral aspects of the Agreement and its consequences for

Canadian life that blur the constitutional image of what the FTA initiative is about.

It does not appear overly generous to concede that most of what the FTA speaks to falls naturally within federal jurisdiction. The Agreement establishes a "free trade area" between the two countries (Article 101) to remove barriers to the movement of goods, services and investment capital across national borders (Article 102). Border measures in general (Chapter 4) are clearly matters of federal jurisdiction as are technical standards (Chapter 6) even without the benefit of trade and commerce jurisdiction.[27] The latter, even on its most conservative interpretation,[28] buttresses federal customs jurisdiction in relation to automotive trade (Chapter 10) and also supports trade in energy (Chapter 9) especially where energy resource production is devoted almost exclusively to export markets.[29] Investment (Chapter 16) also appears on relatively safe ground as foreign investment is firmly in the grip of federal regulation in any event.[30]

Substantive problem areas emerge with respect to wine and distilled spirits (Chapter 8), certain aspects of local market regulation for energy resources and agricultural commodities, and possibly trade in services, relative to, for example, provincial laws regulating consumer protection, insurance schemes, and local business incentives. The Honourable Ian Scott's speech makes the most of all these points.[31]

Other potential problem areas fall away simply because the Agreement does not reach the provinces. The FTA deals with government procurement (Chapter 13), but only those entities already covered by the GATT Code on Government Procurement[32] which Canada entered into at the conclusion of the Tokyo Round of multilateral trade negotiations in 1979. The Canadian commitment does not extend to provincial governments.[33]

Similarly, FTA provisions with respect to financial services (Chapter 17) do not extend to provincially constituted financial institutions. In that regard, it is instructive to note that the constitutional limits of federal jurisdiction in relation to financial services industries in Canada are potentially unlimited; yet the field is also replete with concessions to provincially occupied (concurrent) fields that some of the federal clout may have been lost by default.[34]

The provincial position becomes stronger, however, when we turn to some of the general provisions of the Agreement. As to its coverage, FTA Article 103 declares:

> The Parties to this Agreement *shall ensure* that all necessary measures are taken in order to give effect to its provisions, including their *observances, except as otherwise*

> *provided in this Agreement, by state, provincial and local governments.*[35]

With respect to the basic principle of national treatment (Chapter 5), which pervades the Agreement as a whole, the FTA furnishes a similarly ironclad commitment. In FTA Article 502 the parties promise that:

> [t]he provisions of this chapter regarding the treatment of like, directly competitive or substitutable goods shall mean, *with respect to a province or state, treatment no less favourable than the most favourable treatment accorded by such province or state* to any like, directly competitive or substitutable goods, as the case may be, of the Party of which it forms a part.[36]

To the extent that any substantive areas of the FTA are dependent on the support of provincial jurisdiction to enact the appropriate law, the foregoing statements of general obligation are courageous and, by the same measure, impossible for Ottawa to vindicate under the *Labour Conventions* rule. Nevertheless, Canada will remain responsible under international law for any provincial as well as federal breach of treaty obligations. *Ex post facto* pleas of domestic constitutional limitation hold little currency under the doctrine of international responsibility.[37]

Part III

If the moral of the story is simply that Ottawa should not overcommit itself internationally without provincial agreement and cooperation, then perhaps the conventional wisdom is justified. But it is more than that. Our constitutional structure is such that even after a deal binding at international law is made between Canada and another country, even one for which the agreement of an affected province might have been secured from the provincial government of the day, there is nothing to prevent a province from subsequently walking away.

The consequences of provincial infidelity, intentional or otherwise, have been forcefully brought home to Canada in complaints brought against it under the GATT.[38] In one instance, South Africa challenged an Ontario retail sales tax exemption which discriminated in favour of Maple Leaf gold coins over Krugerrands;[39] in another, the European Community (EC) took Canada to task for the listing, pricing and distribution practices of provincial liquor marketing boards.[40] In both cases, preliminary determinations by

GATT investigating panels found that the targeted provincial laws or practices had given rise to the nullification and impairment of benefits owed by Canada to the named Contracting Parties under the treaty. Arguments that the extent of its obligations were confined to "reasonable measures"[41] well short of waging constitutional warfare with provincial governments have not absolved Canada of liability.

The provincial liquor board complaint, which may still be subject to the possibility of a negotiated settlement independent of the legal finding by the GATT panel,[42] illustrates the point. The EC complaint was generated in part by good faith undertakings offered by Canada and tabled in a provincial "statement of intent" as part of the Canadian position during the Tokyo Round concluded in 1979.[43] While not a legally binding document in itself, the apparent failure of provincial intent to do what was promised[44] did prompt the legal accounting for which Canada will pay.

The liquor marketing example is particularly relevant because the same issue is also subject to FTA concessions on what has been a long-standing trade irritant for the United States as well as EC wine industries. More particularly for present purposes, we are told that "Mr. Peterson Premier of Ontario has consistently said that control over wine production and pricing is the *only clear area of provincial jurisdiction*" implicated in the FTA.[45] It appears that Mr. Peterson's Attorney General has or has had a broader view of provincial capabilities, but even on wine and liquor, the situation is not that clear.

Through a rather untidy constitutional evolution, the social evil of intemperance matured into a local government monopoly for the marketing of alcoholic beverages in each province.[46] In Ontario, for example, the provincial Liquor Control Board (LCBO) has been granted complete powers for the pricing, distribution and marketing of alcoholic beverages under the *Liquor Control Act.*[47] The LCBO is a public corporate entity intended to run at a profit, and it does.[48]

Nevertheless, the actual monopoly enjoyed by the LCBO and every other provincial marketing board is conferred by a federal statutory provision in the *Importation of Intoxicating Liquor Act*, in place since 1928.[49] Parliament abdicated the field in an early gesture of cooperative federalism, but presumably could rescind the import monopoly at the stroke of a pen and a vote in Parliament.

Whether Ottawa would ever want to take such a step in political terms is entirely another matter. Even if it did come to that, the shared field would still permit provincial regulation of local commerce, inclusive of all resale of alcoholic beverages *in* the province. And Canada may, if not inevitably, fall short of its obligations under the FTA. One thing is clear; neither level of government would benefit from the mess that could ensue.

Part IV

The constitutional strength of provincial opposition to the FTA will turn on the ability of a legal challenge to isolate the Agreement into its components. If one or more of these smack sufficiently of provincial jurisdiction to attract the label of *ultra vires*, parallel federal legislation implementing that aspect of the Agreement will fall. This is precisely the tactic contemplated by the recent resolution of the Ontario Legislature condemning the FTA:

> . . . the Legislative Assembly of the Province of Ontario opposes this agreement as detrimental to Canada's sovereignty and economic interests, and *will not be bound to implement those aspects which fall under provincial jurisdiction.* We urge the Parliament of Canada to reject the agreement.[50]

Assuming that provincial aspects are found, nothing is gained for the challenging province unless the subject matter is exclusively provincial in content. It has been long understood that "subjects which in one aspect and for one purpose fall within section 92, may in another aspect and for another purpose fall within section 91."[51] Professor William Lederman has characterized this particular Canadian constitutional dilemma as resolvable through a process of judicial reasoning "on the relative importance of the federal features and the provincial features of the challenged law in contrast to one another."[52] In the result, if federal and provincial aspects are competitive in conflicting federal and provincial laws and the conflict is clear, the doctrine of federal paramountcy holds sway.[53]

Contemporary paramountcy doctrine takes a very strict view of what amounts to a conflict for purposes of invalidating a provincial statute.[54] Such liberality, however, is of no assistance in dispensing with any part of a competing federal scheme if Parliament attempts full implementation of the FTA on its own.

The potential strength of the federal position may lie in dealing with the Agreement and its implementation as a non-severable organic whole. That is certainly a tenable perspective from the Canada-U.S. free trade negotiations *per se*; mutually interdependent concessions make it very much of an all-or-nothing affair.[55] The more it is viewed in that light, the stronger the federal position becomes. My reasons for this conclusion are drawn largely from comparatively recent revelations concerning the general trade and commerce power as well as the prospect for a federal external affairs power which I have already touched on.

Provincial subject matter jurisdiction which invites constitutional scrutiny of comprehensive federal implementing legislation centers on property and civil rights (s.92(13)) and matters of a local and private nature in the province (s.92(16)). Together, they amount to a local mandate for peace, order and good government. Provincial powers over taxation, and the recently conferred regulatory powers over natural resource management[56] complete the picture.[57]

As noted above, federal subject matter jurisdiction is ironclad with respect to particular aspects of the FTA, but none of these offer a general justification for comprehensive federal implementation that would obviate the necessity of confronting the rule in *Labour Conventions*. That doctrine, and the federal principle it may be said to uphold, clearly takes the triviality out of provincial opposition to the FTA.

However, section 91(2) of the *Constitution Act, 1867* seems to have a new potential. Here I refer to the separate opinion by the present Chief Justice of Canada in the *Canadian National Transportation* case,[58] decided in 1984. This development is welcome and perhaps unusual given the history of the Trade and Commerce power in Canada.[59] On that score, a little background is useful.

The constitutional grant to Parliament of jurisdiction over the "Regulation of Trade and Commerce," expansive on its face, never really existed in practice. Judicial preoccupation with notions of symmetrical federalism, in preference to nation building, suggested from the beginning a perhaps narrower view than the Founding Fathers originally had in mind.

In *Citizens Insurance Co.* v. *Parsons*,[60] the Privy Council established three categories of subject matter appropriate to the jurisdiction conferred on Parliament under section 91(2). Sir Montague Smith postulated that the headings "would include political arrangements in regard to trade requiring the sanction of parliament, regulation of trade in matters of inter-provincial concern, and it may be that they would include general regulation of trade affecting the whole dominion."[61] The *Parsons* rationale sought to narrow section 91(2) by relying on the particularity of other enumerated heads of power in the Constitution as mutually modifying (i.e., qualifying) language to the otherwise open-ended character of the section.[62]

The first branch of the *Parsons* test, interprovincial and foreign trade, has dominated trade and commerce jurisprudence. Sir Lyman Duff was the primary architect of a judicial method I have analyzed elsewhere in terms of "specific transaction analysis."[63] Taking the cue from Mr. Justice and then Chief Justice Duff,[64] the Supreme Court of Canada has characterized the issue of regulatory competence under section 91(2) in terms of the kinds of transactions reached by the challenged legislation. Federal authority to regulate the "flow of commerce," as distinguished from particular trades in the province, begins only when a given transaction ceases to be " local" in the sense that it reaches across a provincial or national boundary.[65] Federal regulatory competence similarly ceases, it appears, when commodities again become the subject of transactions exclusively local in character.[66]

In the result, the governing approach to interprovincial and foreign commerce has left little room for federal claims to comprehensive regulatory competence over any business or trade in a particular commodity, even where a preponderance of the business subject to regulation might be interprovincial or transnational in character.[67] There has been a gradual trend to liberalization in market sectors which can be characterized almost exclusively in terms of interprovincial export trade, for example, wheat,[68] certain natural resources[69] and energy.[70] Nevertheless, the Supreme Court of Canada has remained sensitive to Chief Justice Duff's original concerns; where difficulties arise, the courts still evince a marked preference for federal-provincial autonomy and cooperation in national regulatory schemes:[71] shades of *Labour Conventions*.

Most of this plays nicely into the hands of any provincial government that wants to rend the fabric of a federal scheme which extends to local matters in conjunction with otherwise *intra vires* objectives, in this instance, the establishment of a free trade area with the United States. So, on the basis of what has gone before, the Attorney General of Ontario has some basis for constitutional bellicosity.

But the story is not quite over. The second branch of *Parsons*, "general regulation of trade affecting the whole Dominion,"[72] is not similarly constrained by the transactions reached by a challenged regulatory scheme. Unfortunately, however, it has also been difficult to imagine under what specific circumstances general regulatory jurisdiction would apply, especially in the event of a conflict with existing provincial legislation.

The general trade and commerce power was applied twice by the Privy Council, once in upholding federal legislation defining the powers of federally incorporated companies,[73] and again with respect to national trademarks.[74] The dimensions of the general trade and commerce power, however, were never adequately explained in either judgment. Rather, the Privy Council said only that Parliament was entitled to address a "question of general interest throughout the Dominion."[75]

Chief Justice Duff had been presented with an early opportunity to elaborate on the general trade and commerce power under section 91(2) in the *Board of Commerce* case,[76] but instead rejected it as a dangerous and unmanageable encroachment on local autonomy. Regulation in the general interest, in the Chief Justice's view, did not extend to regulatory standards with respect to local trades, even if such a program were to be implemented nationally.[77]

Many years later, a majority of the Supreme Court was still expressing similar views on the limits of federal power in the *Labatt Breweries* case.[78] There the Court invalidated national product identification standards in relation to the marketing of beer.[79] Given that the localized production of beer precluded a flow of commerce justification for federal regulation, Mr. Justice Estey considered and rejected the use of a general trade and commerce rationale. Mr. Justice Estey basically followed the Duff formula in concluding that "[w]hat clearly is not of general national concern is the regulation of a single trade or industry,"[80] such as the production of beer.

Labatt Breweries appeared to confirm the illusory character of the general trade and commerce power; but then came *Canadian National Transportation*.[81] The merits of this case had nothing to do with trade and commerce *per se*, but became a vehicle for Mr. Justice Dickson (as he then was) to join with the majority to affirm the prosecutorial authority of the federal Attorney General.[82]

Mr. Justice Dickson's characterization of the second branch in *Parsons* expressly affirmed Mr. Justice Estey's opinion in *Labatt Breweries*, with which Mr. Justice Dickson admits he concurred.[83] Nevertheless, His Lordship disavowed that *Labatt Breweries* necessarily or properly supported the Duff position in *Board of Commerce* that valid federal regulations could not under any circumstances take the form of orders directed at local trades in the "general interest":

> Every general enactment will necessarily have some local impact, and if it is true that an overly literal conception of "general interest" will endanger the very idea of the local, there are equal dangers in swinging the telescope the other way around. The forest is no less a forest for being made up of individual trees.[84]

If the Duff analysis holds, "then," Mr. Justice Dickson answers, "no economic legislation could ever qualify under the general trade and commerce power."[85] This proposition had been a practically (if not theoretically) correct conclusion to draw with respect to section 91(2) until Mr. Justice Dickson's intimation to the contrary.

For Mr. Justice Dickson, the regulation of particular businesses or trades, which still lies beyond federal power, changes character "when what is at issue is general legislation aimed at the economy as a single integrated national unit rather than as a collection of separate local enterprises."[86] When the qualitative distinction is appreciated with the required precision, constitutional objections to the general regulation of trade allegedly interfering with particular businesses or trades in a province – "individual trees" – may be met and answered in favour of federal regulatory competence to maintain the whole "forest."

Out of this reasoning, Mr. Justice Dickson identified five criteria by which a federal enactment might be characterized either as a colourable attempt to regulate a bundle of local trades or as general regulation of the national economy. The first three are borrowed from the late Chief Justice Laskin[87] and the last two are his own. In support of federal jurisdiction we should look for:[88]

- the presence of a national regulatory scheme
- the ongoing supervision of such a scheme by a federal regulatory agency
- concern with trade in general rather than with an aspect of a particular business
- the fact that the provinces jointly or severally would be constitutionally incapable of passing such an enactment
- the perception that failure to include one or more provinces or localities would jeopardize successful operation in other parts of the country.

If we apply these criteria to the leading features of the FTA what emerges? Well, it is for Parliament to come up with a comprehensive statutory framework. If that framework is tied together like the Agreement, we will have a national regulatory scheme for free trade with the United States. There is also ongoing supervision pursuant to the institutional provisions of the FTA (Chapter 18). We can say further that the focus of the Agreement is trade in general, notwithstanding exceptions to its coverage.[89] And no one will suggest that the provinces jointly or severally could implement anything like the FTA. Finally, there exists a very real danger that one or more recalcitrant provinces could jeopardize the entire scheme, as well as its successful operation in other parts of the country.

The foregoing is a cursory application of tentative law, but it may be a way for the future. The fit is persuasive and should suggest caution to provincial government lawyers as well as give some measure of confidence to the Department of Justice. Of course, the *Canadian National Transportation* approach to general trade and commerce has still to receive approval from a majority of the Supreme Court of Canada, but it may be so blessed in the near future.[90] If that proves to be the case and the foregoing application of the Dickson test is vindicated, then Ottawa may have a full answer and defence for statutory implementation of the FTA, without the need for the deeper constitutional rethinking which I have suggested is long overdue.

Conclusion

Where to from here? Well, with respect to the future of the FTA, all of the foregoing may prove to be unnecessary tilting at windmills. The Mulroney government says it has jurisdiction; it would be somewhat contradictory for Ottawa to question the constitutionality of federal implementing legislation in a reference to the Supreme Court of Canada. However, the FTA is itself a spiritual if not practical contradiction to the other major policy achievement of the Mulroney government in the Meech Lake Constitutional Accord.[91] So anything is possible.

It is equally open to the Government of Ontario or any other province to refer whatever questions they wish on the constitutionality of the FTA to their respective court of appeal from which the reference would likely go to the Supreme Court of Canada. The other possibilities are for a province or private parties litigant to challenge the federal implementing statute(s) after the law is in place.

Any province choosing to take on Ottawa over free trade has a good basis in conventional constitutional wisdom to be confident of credible legal arguments. The strength of these depends in large measure on the ancient but effective tactical principle of "divide and conquer." Whether it can be effectively applied, however, will turn on the kind of target Ottawa offers. An integrated federal scheme will be a much tougher target than random statutory amendments of existing laws: "united it may stand." Each side gets a rallying cry, but the provinces should understand that, if they decide to do battle on this issue, they could lose a good deal more than simply their alleged veto over free trade.

So, we will have to wait and see. The "implementation controversy" over Canada-United States free trade may be resolved – if indeed it ever becomes full-blown – without reaching the more basic constitutional deficiency in relation to the general subject matter of external affairs, an issue also addressed in the controversy. That is a tougher argument which Ottawa has always tried to avoid in the past. Will this be the time to face it? Given the existence of a viable alternative, probably not. Ottawa will again pursue the tactics of avoidance if it possibly can. And so may the provinces. But rest assured, the question will come around again. The next time or sometime, there will be no other way out.

Notes

1. See *Canada-United States Free Trade Agreement*, "Final Text" (19 December 1987) [hereinafter FTA]; see also FTA, "Synopsis" (10 December 1987); FTA, "Summary: Elaborations and

Clarifications to the Elements of the Agreement as Reflected in the Legal Text" (10 December 1987).

2. See U.S.C. art. I (Congressional powers), and art. II (Executive power in the office of the President). See generally, L. Henkin, *Foreign Affairs and the Constitution* (New York: Norton, 1975).

3. The Senate has been repeatedly criticized as either an unnecessary institution of government in contemporary Canada or one badly in need of reform to serve its orginal purpose of effective representation for regional interests in federal lawmaking. See Watts, "Second Chambers in Federal Political Systems" in *The Conferation Challenge*, vol. 2 (1970) at 315; R.A. MacKay, *The Unreformed Senate of Canada*, rev'd. ed. (Toronto: McClelland and Stewart, 1963); D. Smiley, "Central Institutions" in S.M. Beck & I. Bernier eds, *Canada and the Unfinished Agenda*, vol. 1 (Montreal: Institute for Research on Public Policy, 1983) 23 at 60-66.

   However, with respect to the reform issue, the entrenched constitutional position of the Upper Chamber (*Constitution Act, 1867*, (U.K.), 30 & 31 Vict., c. 3, ss. 21-36) was confirmed even before enactment of the *Constitution Act, 1982* (being Schedule B of the *Canada Act 1982* (U.K.), 1982, c. 11, ss. 38, 41, 42). See *Reference Re Legislative Authority of Parliament to Alter or Replace the Senate* (1979), [1986] 1 S.C.R. 54, 102 D.L.R. (3d) 1. And it remains true that, with its power to pass upon all bills from the House before they become law, the Upper House can certainly obstruct the agenda of the government of the day, as illustrated by its recent delay in passing the controversial patent drug bill, C-22, *An Act to amend the Patent Act and to provide for certain matters in relation thereto* (S.C. 1987, c. 41). (House of Commons: lst reading Nov. 7, 1986; 2nd reading Dec. 8, 1986; 3rd reading May 6, 1987; Senate: lst reading May 7, 1987; 2nd reading June 25, 1987; 3rd reading August 13, 1987; Royal Assent: Nov. 19, 1987). Nevertheless, it goes too far to say that the constitutionally valid powers of the Senate can be exercised to their fullest in the Canadian political system when their effect is to negate the representative democratic will of the people emanating from the House of Commons. Even in the case of a Senate hostile to the government of the day, "it is accepted by opposition as well as government senators that the appointive nature of the Senate must necessarily make its role subordinate to the elective House. The result is that very few government bills are rejected or substantially amended by the Senate." P.W.

Hogg, *Constitutional Law of Canada*, 2d ed. (Toronto: Carswell, 1985) at 201.

4. See discussion in H.S. Fairley, "Jurisdiction Over International Trade in Canada" in E. Carasco & M. Irish eds, *The Legal Framework for Canada-United States Trade* (Toronto: Carswell, 1987) 131 at 135-38; Hogg, *supra*, note 3 at 332-34, 339-40.

5. *A.G. Canada* v. *A.G. Ontario (Labour Conventions)* (1937), [1937] A.C. 326, [1937] 1 W.W.R. 299, [1937] 1 D.L.R. 673 (P.C.) [hereinafter *Labour Conventions* cited to A.C.].

6. See generally, R. Simeon, *Federal-Provincial Diplomacy: The Making of Recent Policy in Canada* 2d ed. (Toronto: Toronto Press, 1973); D. Smiley, *Canada in Question: Federalism in the Eighties* 3d ed. (Toronto: McGraw-Hill Ryerson, 1980) at 91-119.

7. For a critique of existing approaches to cooperative federalism in relation to international trade issues, see: H.S. Fairley, "Constitutional Aspects of External Trade Policy" in M. Krasnick Res. Coord., *Royal Comm'n Econ. Union Dev't Prosp. Can. Res. St.: Case Studies in the Division of Powers*, vol. 62 (1986) 1 at 25-30.

8. Originally enacted (U.K.), 30 & 31 Vict., c. 3; renamed in the Schedule to the *Constitution Act, 1982*, Item No. 1.

9. The Supreme Court of Canada has suggested that Canada acquired international personality as early as 1923. See *Reference Re Amendment of the Constitution of Canada (Nos. 1, 2 and 3), (Patriation Reference)* (1981), [1981] 1 S.C.R. 753, 125 D.L.R. (3d) 1 at 44, Laskin C.J., Dickson, Beetz, Estey, McIntyre, Chouinard and Lamer JJ. [hereinafter *Patriation Reference* cited to D.L.R.].

10. (U.K.), 22 Geo. 5, c.4.

11. See *Bank of Toronto* v. *Lambe* (1887), 12 App. Cas. 575 at 586 (P.C.), Lord Hobhouse: "There Lordships have to construe the express words of an Act of Parliament . . . ."

12. For elaboration of this argument, see Fairley, *supra*, note 4 at 138-41.

13. Lord Wright, who sat as a member of the Privy Council (the rules of which permitted no dissenting opinions), subsequently disclosed his opposition to the opinion expressed by Lord Atkin. See Lord Wright, "Rt. Hon. Sir Lyman Poore Duff, G.C.M.G. 1865-1955" (1955) 33 Can. Bar Rev. 1123 at 1125-29; see also F.R. Scott, "Lord Wright's Undisclosed Dissent?" (1956) 34 Can. Bar Rev. 114.

14. *Labour Conventions, supra*, note 5 at 351.

15. *Ibid.* at 354.

16. *Ibid.*

17. Cf. some of the vast literature critizing the result in *Labour Conventions*: G.L. Morris, "The Treaty-Making Power: A Canadian Dilemma" (1967) 45 Can. Bar Rev. 478; MacDonald, *supra*, note 30; F.R. Scott, "The Consequences of the Privy Council Decisions" (1937) 15 Can. Bar Rev. 485; G.J. Szablowski, "Creation and Implementation of Treaties in Canada" (1956) 34 Can. Bar Rev. 28; G.V. LaForest, "The Labour Conventions Case Revisted" (1974) 12 Can. Y.B. Int'l L. 137; I.C. Rand, "Some Aspects of Canadian Constitutionalism" (1960) 38 Can. Bar Rev. 135 at 142-43. Quebec scholars go the other way and use *Labour Conventions* as a vehicle for establishing provincial international personality to directly enter into treaties in fields of provincial jurisdiction. See J.Y. Morin, "La Personnalité Internationale du Québec" (1984) R.Q.D.I. 163.

18. For the strongest summary and defence of the federal principle to date, see *Patriation Reference, supra*, note 9 at 58, Martland and Ritchie JJ. (dissenting) : "The implications of that principle are clear. Each level of government should not be permitted to encroach on the other, either directly or indirectly . . . ." See also *Ibid.* at 49-79; cf. W.R. Lederman, Comment (1982) 27 McGill L.J. 527.

19. I refer to those (i.e., Martland and Ritchie JJ. in *Labour Conventions, supra*, note 18) who hold to the idea of federalism as defining autonomous spheres of governmental action, which Professor Wheare described most eloquently as "the method of defining powers so that the general and regional governments are each, within a sphere, co-ordinate and independent." (K.C.

Wheare, *Federal Government* 4th ed. (London: Oxford University Press, 1946) at 10).

20. For comparative insights see, for the United States: *United States* v. *Curtiss-Wright Export Corp.* (1936), 299 U.S. 304; and for Australia: *Commonwealth of Australia* v. *State of Tasmania (Franklin River Dam)* (1983), 46 A.L.R. 625 (Australia H.C.).

21. See *Francis* v. *The Queen* (1956), [1956] S.C.R. 618, 3 D.L.R. (3d) 159; *MacDonald* v. *Vapour Canada Ltd* (1975), [1977] 2 S.C.R. 134, 7 N.R. 477; Cf. *Reference Re Ownership of Off-Shore Mineral Rights* (1967), [1967] S.C.R. 792, 65 D.L.R. (2d) 353; *Reference Re the Seabed and Subsoil of the Continental Shelf Offshore Newfoundland* (1983), [1984] 1 S.C.R. 86, 5 D.L.R. (4th) 385 [hereinafter *Hibernia Reference* cited to S.C.R.]. On the significance of the *Hibernia Reference*, see discussion in H.S. Fairley, "Developments in Constitutional Law: the 1983-84 Term" (1985) 7 Sup. Ct L. Rev. 63 at 69-78.

22. *Constitution Act, 1867* (U.K.), 30 & 31 Vict., c.3, s.91 [hereinafter *Constitution Act, 1967*].

23. *Labour Conventions, supra*, note 5 at 351.

24. It is fully developed in H.S. Fairley "Canada, External Affairs and the Constitution: A Theory for Judicial Review" (MS. Doctorate/Judicial Science, Faculty of Law, Harvard, April 1987) [unpublished]. (Catalogued and on file at the Harvard Law School Library and currently in revision with a view to publication).

25. See Statement by the Honourable Ray Hnatyshyn, Minister of Justice and Attorney General of Canada, reprinted in Canada, *House of Commons Debates*, 33d Parl. 2d Sess. (16 December 1987) at 11 847:

> The treaty is within the legal competence of the Government of Canada on behalf of the people of Canada. We are entitled, under the Constitution of this country, to enact this treaty. In fact, we have indicated on many previous occasions, *we have every legal right to put into effect all the provisions of the treaty*. (emphasis added)

26. See "Notes for Remarks" by the Honourable Ian Scott, Attorney General to the Canadian Bar Association/Ontario, Corporate and

Business Law Section (Toronto, 15 December 1987). The "jackboot" metaphor is mine, but Mr. Scott's point is no less forcefully made.

27. For example, *Constitution Act, 1867, supra*, note 22 at ss. 91(22) (Patents), 91(23) (Copyright) and 122 (Customs).

28. See *infra*, notes 60-80 and accompanying text.

29. The addition of section 92A to the *Constitution Act, 1867* in 1982 should not undercut any federal legislation implementing energy export guarantees in the FTA. See discussion in Fairley, *supra*, note 7 at 21-22; W.D. Moull, "Section 92A of the *Constitution Act, 1867*" (1983) 61 Can. Bar Rev. 715; J.B. Ballem, "Oil and Gas Under the New Constitution" (1983) 61 Can. Bar Rev. 547.

30. For example, *Foreign Investment Review Act*, S.C. 1973, c. 46, as rep *Investment Canada Act*, S.C. 1985, c. 20, s. 46. Note: *Foreign Investment Review Act* came into force on 9 April 1974 and *Investment Canada Act* on 1 July 1985.

31. *Scott, supra*, note 26 at 11-17.

32. GATT Doc. MTN/NTM/W/211/Rev. 2; (1979) 18 Int'l Leg. Mats 1052, consolidated in GATT, *Agreement on Government Procurement* (Geneva, 1979).

33. For analysis see, de Mestral, "The Impact of the GATT Agreement on Governmental Procurement in Canada" in J. Quinn & P. Slayton eds, *Non-Tariff Barriers After the Tokyo Round*, Proceedings of a conference sponsored by the Canada-United States Law Institute, London, Ontario (10 May 1980), (Montreal: Institute for Research on Public Policy, 1982) at 171.

34. For discussion see, E.S. Binavince & H.S. Fairley, "Banking and the Constitution: Untested Limits of Federal Jurisdiction" (1986) 65 Can. Bar Rev. 328 at 349-65.

35. (Emphasis added).

36. (Emphasis added).

37. See *Treatment of Polish Nationals in Danzig* (Ad. Op.) P.C.I.J. Ser. A/B, No. 44 (1932) at 44: "A State cannot adduce as against

another State its own Constitution with a view to evading obligations incumbent upon it under international law or treaties in force"; see generally, I. Brownlie, *Principles of Public International Law* 3d ed. (Oxford: Clarendon Press, 1979) at 36; L.F.L. Oppenheim, *International Law*, 8th ed. by H. Lauterpacht (London: Longmans' Green, 1955) 337 at 357.

38. *General Agreement on Tariffs and Trade*, done at Geneva (30 October 1947), in force 1 January 1948, 55-61 UNTS 194; for consolidation see GATT, 4 *Basic Instruments and Selected Documents* (Geneva, 1969).

39. See GATT, *Canada-Measures Affecting the Sale of Gold Coins: Report of the Panel* GATT Doc. L/5863 (17 September 1985).

40. See discussion in Fairley, *supra*, note 7 at 25-29; Fairley, *supra*, note 4 at 157-61.

41. See GATT, art. XXIV(I2), which provides: "Each contracting party shall take such reasonable measures as may be available to it to ensure observance of the provisions of this Agreement by the regional and local governments within its territory."

42. The text of the panel determination, reported in the press in November 1987, is still secret as of this writing.

43. The text of the Statement is reproduced in Canada, Industry, Trade and Commerce, *Multilateral Trade Negotiations 1973-1979* (undated) at 98-99.

44. See Fairley, *supra*, note 7 at 27-28.

45. As reported in *The (Toronto) Globe and Mail* (7 January 1988) 4.

46. See *Russell* v. *The Queen* (1882), 7 App. Cas. 829, 2 Cart. 12 (P.C.); *A.G. Ontario* v. *A.G. Canada (Local Prohibition)* (1896), [1896] A.C. 348 (P.C.); *A.G. Ontario* v. *Canada Temperance Federation* (1946), [1946] A.C. 193, 2 W.W.R. 1 (P.C.).

47. R.S.O. 1980, c. 243, s. 3 (outlining the purposes and powers of the Liquor Control Board). See also *Liquor Control and Licencing Act*, R.S.B.C. 1979, c.237; *An Act Respecting the Commission de controle des permis d'alcool* R.S.Q. 1977, c. C.33.

48. For example, for the fiscal year 1982-83 the LCBO had sales of $1 467 296 000 as against operating expenses of $204 142 000; expenses constituted 13.9 per cent of total sales and net income was $523 228 000. See Liquor Control Board of Ontario, *57th Report* (1983).

49. R.S.C. 1970, c. I-14, s. 3(1) (unchanged from S.C. 1928, 18 & 19 Geo. 5, c. 31).

50. Legislative Assembly, *Province of Ontario Votes and Proceedings*, 34th Parl. 1st Sess. (6 January 1988) at 237 (vote: 79 to 27).

51. *Hodge* v. *The Queen* (1883), 9 App. Cas. 117 at 130 (P.C.).

52. W.R. Lederman, "The Concurrent Operation of Federal and Provincial Laws in Canada" (1962-63) 9 McGill L.J. 185. Reprinted in W.R. Lederman, *Continuing Canadian Constitutional Dilemmas* (Toronto: Butterworths, 1981) 250 at 251.

53. See generally, Hogg, *supra*, note 3 at c. 16.

54. See *Multiple Access Ltd* v. *McCutcheon* (1981), [1982] 2 S.C.R. 161, 138 D.L.R. (3d) 1.

55. For a comprehensive overview of all areas of the Agreement see J.D. Richard & R.G. Dearden, *The Canada-U.S. Free Trade Agreement: Commentary and Related Documents* (1988).

56. *Constitution Act, 1867*, s. 92A. See sources cited *supra*, note 29.

57. For elaboration see Fairley, *supra*, note 7 at 18-22.

58. *A.G. Canada* v. *Canadian National Transportation Ltd* (1982), [1983] 2 S.C.R. 206, 3 D.L.R. (4th) 16 [hereinafter *C.N. Transportation* cited to D.L.R.].

59. See the comparative analysis in A. Smith, *The Commerce Power in Canada and in the United States* (Toronto: Butterworths, 1963).

60. (1881), 7 App. Cas. 96, 1 Cart. 265 (P.C.) [hereinafter *Parsons* cited to App. Cas.].

61. *Ibid.* at 113.

62. *Ibid.* at 109:

> In these cases it is the duty of the courts, however difficult it may be, to ascertain in what degree, and to what extent, authority to deal with matters falling within these classes of subjects exists in each legislature . . . . It could not have been the intention that a conflict should exist; and in order to prevent such a result, the two sections must be read together, and the language of one interpreted, and where necessary, modified by that of the other.

63. See Fairley, *supra*, note 7 at 8-11.

64. See respectively, *R.* v. *Eastern Terminal Elevator Co.* (1925), [1925] S.C.R. 434 at 446, [1925] 3 D.L.R. 1; *Reference Re Natural Products Marketing Act, 1934* (1936), [1936] S.C.R. 398, [1936] 3 D.L.R. 622 [hereinafter *Natural Products* cited to D.L.R.]; see generally, G. Le Dain, "Sir Lyman Duff and the Constitution" (1974) 12 Osgoode Hall L.J. 261 at 293-308.

65. For example, *A.G. Manitoba* v. *Manitoba Egg and Poultry Ass'n* (1971), [1971] S.C.R. 689, 19 D.L.R. (3d) 169 (provincial regulation of interprovincial transactions in eggs *ultra vires*); *Burns Foods Ltd* v. *A.G. Manitoba* (1973), [1975] 1 S.C.R. 494, 40 D.L.R. (3d) 731 (provincial regulation of interprovincial trade in hogs *ultra vires*).

66. *Dominion Stores Ltd* v. *R.* (1979), [1980] 1 S.C.R. 844, 106 D.L.R. (3d) 581; *Canadian Federation of Agriculture* v. *A.G. Quebec (Margarine Reference)* (1948), [1949] S.C.R. 1 *(sub nom. Reference Re Validity of Section 5(a) of the Dairy Industry Relief Act)* (1948), [1949] 1 D.L.R. 433, aff'd (1951), [1951] 1 A.C. 179, [1950] 4 D.L.R. 689 (P.C.).

67. For example, *Carnation Co.* v. *Quebec Agricultural Marketing Bd.* (1968), [1968] S.C.R. 238, 67 D.L.R. (2d) 1 (upholding constitutionality of provincial marketing plan fixing minimum prices for milk paid to local producers, notwithstanding preponderance of production aimed at interprovincial and export trade).

68. For example, *Murphy* v. *C.P.R.* (1958), [1958] S.C.R. 626, 15 D.L.R. (2d) 145 (validity of *Canadian Wheat Board Act* re:

compulsory purchasing of grain destined for extraprovincial markets sustained); *R.* v. *Klassen* (1959), 20 D.L.R. (2d) 406, 29 W. W.R. 369 (Man. C.A.) (leave to appeal to Supreme Court of Canada refused November 30, 1959) (*Canada Wheat Board Act* upheld in application to local work).

69. See *Central Canada Potash Co.* v. *Saskatchewan* (1977), [1979] 1 S.C.R. 42, 88 D.L.R. (3d) 609.

70. See *Caloil Inc.* v. *A.G. Canada* (1970), [1971] S.C.R. 543, 20 D.L.R. (3d) 472 (upholding valid federal prohibition on sale of imported oil west of the Ottawa Valley); *Canadian Industrial Gas & Oil Ltd* v. *Saskatchewan* (1976), [1978] 2 S.C.R. 545, 80 D.L.R. (3d) 449 (invalidating provincial wellhead pricing and production controls *viz.* interprovincial and export pipeline grid).

71. See *Agricultural Products, supra*, note 64 (federal adjustment levies and quotas on local production of eggs *ultra vires*). Pigeon J. for the majority concluded at 325:

> I can find no basis for the view that there must be a division of authority at the stage of production between what will be going into intraprovincial and what will be going into extraprovincial trade .... Under the present circumstances such farms are, like any other farms, local undertakings subject to provincial authority, irrespective of the destination of their output ....

72. *Parsons, supra*, note 60 at 113.

73. *John Deere Plow Co.* v. *Wharton* (1914), [1915] A.C. 330, 18 D.L.R. 353 (P.C.) [hereinafter *John Deere* cited to A.C.].

74. *A.G. Ontario* v. *A.G. Canada (Canada Standard Trade Mark)* (1937), [1937] A.C. 405, [1937] 1 D.L.R. 702 (P.C.).

75. *John Deere, supra*, note 73 at 340, Viscount Haldane L.C.: "For if it be established that the Dominion Parliament can create such companies, then it becomes a question of general interest throughout the Dominion in what fashion they should be permitted to trade."

76. *Re Board of Commerce Act and Combines and Fair Prices Act of 1919* (1920), 60 S.C.R. 456, 54 D.L.R. 354.

77. See analysis in LeDain, *supra*, note 64 at 293-308.

78. *Labatt Breweries of Canada Ltd* v. *A.G. Canada* (1979), [1980] 1 S.C.R. 914, 110 D.L.R. (3d) 594, Estey J. (Martland, Dickson, Beetz and Pratte JJ. concurring) [hereinafter *Labatt Breweries* cited to D.L.R.].

79. *Food and Drugs Act*, R.S.C. 1970, c. F-27, s. 6; *Food and Drug Regulations*, C.R.C., c. 870, s. B.02.134.

80. *Labatt Breweries*, *supra*, note 78 at 623.

81. *Supra*, note 58.

82. For a detailed discussion of both aspects of the case see Fairley, *supra*, note 21 at 85-93 (divided powers over prosecutorial discretion), and at 98-104 (general regulation of trade).

83. *C.N. Transportation*, *supra*, note 58 at 61 (citing Estey J. in *Labatt Breweries*, *supra*, note 78 at 624).

84. *Ibid.* at 61.

85. *Ibid.* at 61 and 70.

86. *Ibid.* at 62.

87. *Ibid.*, citing Laskin C.J. in *MacDonald* v. *Vapour Canada Ltd*, (1975), [1977] 2 S.C.R. 134, 66 D.L.R. (3d) 1 at 25-26.

88. *Ibid.*

89. See FTA, c. 12, arts 1201-05 (for example, FTA, art. 1204 *viz.* Beer and Malt Containing Beverages).

90. The resurrection of general trade and commerce has already attracted a following in the lower courts: *BBM Bureau of Measurement* v. *Director of Investigation and Research* (1984), 9 D.L.R. (4th) 600 (F.C.A.D.) (federal combines prohibition of "tied selling" arrangements *intra vires* per general trade and commerce); *Rocois Construction Inc.* v. *Quebec Ready Mix Inc.* (1985), 25 D.L.R. (4th) 373 (F.C.A.D.) (leave to appeal granted, Can. Sup. Ct., Feb. 3, 1986); The following two cases raise the same issue as *Rocois*: *Dominion Ready Mix Inc.* v. *A.G. Canada* (1985), [1986] R.D.J. 45 (Que. C.A.) (leave to appeal granted,

S.C.C., Feb. 3, 1986); *City National Leasing Ltd* v. *General Motors of Canada Ltd* (1986), 28 D.L.R. (4th) 158 (Ont. C.A.) (leave to appeal granted, S.C.C., Feb. 3, 1986).

91. See Government of Canada, *A Guide to the Meech Lake Accord* (August, 1987); generally, B. Schwartz, *Fathoming Meech Lake* (Winnipeg: Legal Research Institute of the University of Manitoba, 1987).

Constitutional Judicial Review and the Free Trade Agreement

W.R. Lederman

My concern today is one particular aspect of the Canada-U.S. Free Trade Agreement (FTA) as it relates to the constitutional law of Canada. I refer to Chapter 19 of the FTA, "Binational Dispute Settlement in Antidumping and Countervailing Duty Cases." This chapter provides that final antidumping or countervailing duty determinations made by the competent domestic investigating authority of either party shall be subject to binational panel review as specified in Article 1904. With respect to final determinations by such a binational panel, two further provisions are made: (1) there shall be *no* further appeal by either party to the domestic courts of the importing party (see Article 1904.11) and, (2) either party may resort to an "extraordinary challenge procedure" to review "final" panel decisions which is, in effect, an appeal from panel decisions to a special binational appeal tribunal (an "extraordinary challenge committee"), comprised of three members. This committee may affirm or vacate original final binational panel decisions (Article 1904.13 and Annex 1904.13). Affirmations, of course, are effective and end the matter. If a panel decision is vacated, then a new panel is constituted and the binational dispute-resolution procedure starts again. In any event, intervention by or resort to the regular domestic court system of either Canada or the United States is altogether precluded.

This exclusion causes a constitutional problem for Canada. Normally, domestic superior courts are constitutionally entitled to engage in the final review of decisions of domestic administrative bodies to ensure their compliance with statutory grants of power, or their compliance with fundamental fairness in procedures. While this review is quite limited, it is important. This type of review can be characterized as judicial review designed to vindicate and uphold the rule of law itself. Privative clauses in statutes purporting to preclude this review have so far been ruled unconstitutional by the Supreme Court of Canada. If Chapter 19 of the FTA is implemented by a statute of the Canadian Parliament, must it not also include such a privative clause? I think it would have to. Moreover, I believe that in these special circumstances the privative clause would be constitutionally valid.

A close look at the provisions for the extraordinary binational challenge committees (Annex 1904.13) indicates that *each such committee is itself a superior court* based on what one may call "the *Act of Settlement* model." Furthermore, the final review powers of these committees are confined to basic rule of law issues, precisely as in the domestic context respecting the regular domestic superior courts. In other words, the extraordinary challenge committee under the FTA is a single, binational Canadian-American superior court empowered to ensure compliance with the rule of law as it relates to the relevant terms of the FTA. Within *international* circumstances, one may forcibly argue that the *binational* superior court is the appropriate superior court and that the *domestic* superior courts of either country are inappropriate. Hence, the exclusion of the latter as called for in the FTA is proper.

Of course, when I refer to the Canadian domestic superior courts, I am referring to the provincial trial and appeal courts, the Supreme Court of Canada, the federal trial courts and the Federal Court of Appeal. I hope and indeed presume that the same can be said with regard to U.S. constitutional law since U.S. superior courts, including the federal courts and the Supreme Court of the United States, share the same historical roots and basic character as Canadian superior courts. While I am not an expert on American constitutional law, it seems that Superior Court review is *carefully preserved under Chapter 19 of the FTA when, in effect, a single binational superior court takes the place of the domestic national superior courts of both Canada and the United States*. In this regard, Annex 1904.13 provides as follows:

> The members [of the extraordinary challenge committee] shall be selected from a ten person roster comprised of judges or former judges of a federal court of the United States of America or a court of superior jurisdiction of

> Canada. Each Party shall name five persons to this roster. Each Party shall select one member from this roster and the third shall be selected from the roster by the two members chosen by the Parties or, if necessary, by lot from the roster.

Again, each *committee* of three is a *superior court* for the resolution of the challenge with which it is charged. A rose by any other name still smells as sweet.

The essence of the superior courts—as primary constitutional institutions—is the same in Canada and the United States. This essence resides in the independence of the superior court judges as autonomous decision makers, modelled on the historic English superior courts, especially as these developed on the basis of the *Act of Settlement* of the British Parliament of 1701. This long story cannot be rehearsed here. I refer, therefore, to Article III of the United States Constitution of 1789, the article which still defines and governs the federal court system there, at the apex of which is the U.S. Supreme Court.

Addendum—I have published in detail on the subject of judicial independence several times since 1956, most recently in an essay in (1988) 12 Queen's L.J. 385.

Constitutional Dimensions of the Free Trade Agreement

Patrick J. Monahan

In this country, political issues have a strange and recurring habit of transforming themselves into issues of federalism. The same can be said about the Free Trade Agreement (FTA). Alongside economic considerations, an important emerging question surrounding the FTA is the constitutional competence of the federal Parliament to unilaterally implement it.

Professor Fairley's thoughtful paper provides the context for this important constitutional debate. As he pointed out, although the *Constitution Act, 1867* is silent with regard to the power of the federal government to enter into international agreements, this power can be derived from the imperial Crown's delegation of prerogative powers over foreign affairs to the Governor General of Canada. Professor Fairley further acknowledges that in current Canadian constitutional law, the authority to implement treaties is divided between Parliament and the provinces in accordance with their respective legislative jurisdictions. Within this context, there is very real doubt concerning the authority of the federal Parliament to fully implement the Free Trade Agreement. The extent of this difficulty can be illustrated by an analysis of the purpose and effect of the Agreement in light of the division of powers under the *Constitution Act, 1867*.

The first point to note is that, regardless of the breadth of federal authority to regulate "trade and commerce," the FTA deals substantially and directly with matters falling within provincial jurisdiction.

Secondly, certain framework provisions of the Agreement assume a direct impact on provincial jurisdiction. The "extent of obligations" clause (Article 103) is perhaps key in this regard:

> The parties to this Agreement shall ensure that all necessary measures are taken in order to give effect to its provisions, including their observance, except as otherwise provided in the Agreement, by state, provincial and local governments.

This article can be compared to the obligation under the General Agreement on Tariffs and Trade (GATT) which provides:

> Each contracting party shall take such reasonable measures as may be available to it to ensure observance of the provisions of this agreement by the regional and local governments and authorities within its territory (Article XXIV:12).

Much of the commentary surrounding Article 103 has focused on its reference to "necessary measures" as opposed to the language of "reasonable measures" found in the GATT. The difference, while significant, does not fully reflect the important distinctions between the two. The FTA specifies an important class of measures which are "necessary," namely, the observance of the Agreement by state, provincial and local governments. The federal government, in other words, must *ensure* provincial compliance. This interpretation is confirmed by other sections of the Agreement which specifically provide that the provinces need not comply with particular obligations. Article 601, for example, provides that the obligations regarding technical standards do not apply to the provinces or states, and that "accordingly the Parties need not ensure the observance of these provisions by state or provincial governments."

Article 103, which might be termed the federal "insurance" clause, makes sense only if the Agreement substantially deals with matters within provincial competence. What sort of impact on provincial jurisdiction is contemplated? The Attorney General of Ontario, the Honourable Ian Scott identified a number of important concerns in a speech to the Canadian Bar Association in December 1987:

- provincial laws which, prior to export, require upgrading or processing of a natural resource in Canada may be subject to challenge as improper export restrictions.

- attempts to cut back production of a resource so as to raise the export price in the United States may be subject to challenge.
- consumer protection measures which restrict the right of nonresidents to carry on businesses in the province may be challenged on the basis that they contain restrictions which are greater than necessary to protect consumers.
- the establishment of public insurance schemes, such as comprehensive automobile insurance, will be subject to challenge under the monopolies chapter and will further be subject to a claim of compensation by privately owned companies which might be affected.
- trade-related investment measures such as grants, tax breaks and other incentives may be subject to challenge on the grounds that they constitute unjustifiable discrimination.

In short, Article 103 assumes that the FTA applies to the provinces. Furthermore, a number of provisions in the Agreement illustrate that it is intended to strike at some important areas of provincial jurisdiction.

The federal government is obligated to ensure that provincial governments observe the terms of the FTA. What, in practical terms, does this obligation imply? Suppose a provincial government attempts to establish a comprehensive public automobile insurance scheme, as has already been done in British Columbia, Manitoba and Saskatchewan. It could be argued that the creation of a public monopoly is "tantamount to an expropriation," and that the privately owned companies displaced by the monopoly would be entitled to compensation. Accordingly, the federal government would be obliged to ensure that compensation was paid.

If the federal government were willing to assume this obligation, then no constitutional difficulty would arise. But it is highly unlikely, to say the least, that the federal government would be prepared to bear the enormous cost. It is more likely that the federal government would attempt to coerce the provinces into paying. Indeed, the federal government would be obligated to ensure that payment from the provinces was forthcoming.

It is not entirely clear how the federal government could discharge this obligation. It is possible that Parliament might enact legislation requiring the provinces to compensate companies displaced by public monopolies. If necessary, Parliament could then invoke the doctrine of paramountcy and argue that their legislation renders inoperative any inconsistent provincial law.

Yet merely to state this example demonstrates its constitutional novelty. In this instance, paramountcy would be invoked not merely to render a provincial regulation inoperative; the express purpose of such an initiative would be to directly impose an obligation upon the provincial treasury, and the occasion for the law is the need to render the provincial law inoperative. There is no independent national purpose at work. Moreover, the federal legislation would necessarily go beyond a simple requirement of nondiscrimination and would prescribe the terms and conditions of provincial regulation. As such, the federal initiative would be a direct intrusion into provincial jurisdiction.

Perhaps this example is unrealistic. The federal government may never seek to directly intervene in provincial jurisdiction in this way. The point is, Article 103 is a direct repudiation of the *Labour Conventions* principle. It purports to impose an obligation on the federal government which the Constitution says the federal government cannot discharge.

In his discussion on the federal government's constitutional position, Professor Fairley relies heavily on Chief Justice Dickson's judgment in the *CN Transportation* case. According to Professor Fairley, the criteria established in that case regarding federal authority over the "general regulation of trade affecting the whole Dominion" mesh rather nicely with the Free Trade Agreement.

Even accepting the general plausibility of this argument, Professor Fairley fails to mention an additional consideration, namely the Supreme Court's insistence, across a variety of contexts, on the need to maintain an equilibrium between federal and provincial powers in Canadian constitutional law. This is reflected in the development of the Peace, Order and Good Government power in recent years, specifically the requirement that a "matter" be discrete and limited in scope in order to qualify as a matter attaining "national dimension." Indeed, Chief Justice Dickson in the *CN Transportation* case refers to the need to maintain a balance between the two levels of government in the evolution of the "general trade" power. Given the scope of federal power under the FTA and the potential impact this may have on the provinces, it would be surprising indeed if the Supreme Court were willing to uphold federal implementing legislation under the general trade rubric.

Let me close with this caveat. Until the federal government tables its implementing legislation, it is extremely difficult to arrive at any firm conclusion relating to the constitutional authority in this matter. There are clearly a number of options open to the federal government, and the extent of its intrusion into provincial territory will depend upon which of these options are chosen. One thing at least is clear: the constitutional issue will play a central role in the federal government's calculations in this matter and on the eventual success or failure of the Free Trade initiative in the months ahead.

VIII.

The Great Debate – Will the Free Trade Agreement Affect Canada's Sovereignty?

Sovereignty

Richard G. Lipsey

It is, perhaps, a little embarrassing for an economist to be talking to so august an assembly of lawyers about sovereignty. No doubt, you thought lawyers had the first and last thing to say on the issue. Nonetheless, much of the Great Free Trade Debate that has been going on among lay persons for the last year or more has concerned the effects of the Canada-United States Free Trade Agreement (FTA) on Canada's sovereignty. I use the word sovereignty in the loose sense: the ability to make unilateral decisions to follow various policies judged by the government to be in the national interest.

As Murray Smith and I observed some time ago, there are two types of pressures that may act to erode Canadian sovereignty.[1] The first are pressures (exerted at the bargaining table) to abandon certain policies or to tie our hands against using such policies in the future. These constraints are embodied in the treaty and may be called "direct constraints." The second type arise after the Agreement has been put into effect. Market forces may then be unleashed which constrain the future exercise of policies even though no legal constraints exist. These are the so-called "policy harmonization pressures," and they may be called "indirect constraints." I have discussed these latter pressures at length elsewhere[2], and will therefore confine myself here—as is suitable to the topic of this conference – to a discussion of the issue of what the FTA itself does to Canadian sovereignty by virtue of the conditions it lays down.

The issue of sovereignty has been hotly debated ever since the terms of the Agreement were published. Opponents assert that Canada has seriously restricted its sovereignty in return for no great advantages. Supporters argue that the advantages of the Agreement in increasing access to the market of Canada's major trading partner are great, and that any costs paid in terms of restraints on sovereignty are small.

Preliminaries

Although I am surprised that such a statement is needed, I must point out that since all international agreements restrict sovereignty in one way or another, it is not a valid criticism to point out that a particular treaty restricts sovereignty. The correct evaluation of the sovereignty issue, rather, is to ask whether what Canada gave up and what the United States gave up constitutes a reasonably balanced, mutually beneficial package.

Furthermore, giving up some sovereignty can be in the national interest. The classic example, long studied by economists, concerns "prisoner's dilemma" situations. When these arise, tying one's hands against certain policies leads to an outcome superior to that which arises when each individual nation is free to adopt policies seemingly in its best interest. A well-known application of this principle are the arrangements embodied in the GATT. At any moment, each nation is politically self-interested in raising tariff barriers, taking as given the tariff barriers of the rest of the world. Recognizing this self-interest, each nation raises tariffs unilaterally. The outcome of this competitive process is a high-tariff world that is in no one's self-interest. It is, therefore, in the best interests of all trading nations to restrain their rights to raise tariffs by submitting to an international agreement such as the GATT. The GATT provides a cooperative solution to the prisoner's dilemma – a solution which is superior to the noncooperative strategy of each nation pursuing its own interests.

General Sovereignty Concessions in the Free Trade Agreement

When I look at the Canada-U.S. Free Trade Agreement and ask whether what Canada gave up and what the United States gave up constitutes a mutually acceptable package, I come to several conclusions: (1) Canada gave up some, but not a great deal, of sovereignty; (2) much of what Canada did give up is not of great value;

and (3) Canada gave up much less than opponents to the Agreement would have us believe. Let it not be forgotten that the Americans gave up sovereignty as well. To me, the balance of concessions on sovereignty seem to be very reasonable. I am not sure that Canada gave up much in gross figures. On balance, whatever was given up seems well worth the price of such an historic agreement: one that regularizes trade between the two countries, and one that liberalizes trade beyond anything that could ever be expected from the Uruguay Round of multilateral negotiations.

Canada did, however, significantly relinquish some sovereignty in the investment and energy chapters. There are various views concerning the simple facts of what Canada may have given up and these are wildly at odds with each other. Some say that the Agreement signed away everything that matters; others say it signed away very little. I believe that little was signed away. Again, these disagreements concern matters of fact. To assess them, the words of the Agreement cannot be read in a vacuum. The intentions of the Trade Negotiations Offices on both sides of the border matter, as do the contexts of all words used within the precedents of the GATT.

Specifics in the Agreement

So let us look at Canadian sovereignty from the perspective of the chapters on investment and energy.

Investment

When one thinks of the heated debate that has surrounded the chapter on investment, it can come as a shock to read the actual text, the bulk of which concerns the establishment of generally accepted rules of international investment. This is in the self-interest of any country that is a major foreign investor, as are both the United States and Canada.

According to Article 1607.3, Canada reserves the right to review direct acquisitions of Canadian firms by Americans, but the threshold for that review is raised in four steps from the present $5 million to $150 million. Review of indirect acquisitions, where ownership of a firm located in Canada is transferred from one foreign owner to another, is to be phased out over the same time period. Limitations of review of takeovers will *not* extend to firms in the gas, oil and uranium industries.

Giving up the right to review indirect acquisitions does not seem to compromise legitimate national objectives since the investment is already owned abroad. Moreover, giving up the right to review direct middle-sized acquisitions does not seem to be a major policy restriction in light of the following:

- Since its inception, Investment Canada has not reviewed a single case in the range from $5 million to $150 million.
- Canada is a major foreign investor and, as such, its national interest lies more in establishing fair rules of national treatment for its firms investing in the United States, either through takeovers or the establishment of new U.S. subsidiaries, than to restrict foreign capital coming into Canada.
- About three quarters of total nonfinancial capital in Canada is still reviewable under the terms of the Agreement and this includes all of the large takeovers that usually become the object of national concern.

In Article 1603, the two countries agree that performance requirements (such as those imposed by the FIRA) on foreign companies coming into Canada in the 1970s, will no longer be used. This is not, I think, a great concession since such requirements have not been imposed for many years because of their tendency to discourage foreign capital which Canada is trying to attract. Furthermore, it is generally believed that such requirements are not consistent with the GATT, insofar as they affect international trade and would not have withstood a GATT challenge. Nonetheless, it is true that the ability of a future government to bring back performance requirements is restricted. In this case, the Agreement encourages free market determination rather than government intervention in making business decisions.

The prevailing view is that markets matter more than government activity in creating wealth. All governments, especially those which have tried most to intervene in economic matters, have come to believe that markets must be given more scope. If a government is to make international agreements, it must reflect these views. It seems farfetched to say that these agreements will restrict some distant and unforeseen situation, when Canadian governments want to revert to the political economy of modern-day Eastern Europe. If the world really wants to go that route, Canada will change its arrangements; commitments are only temporary. In my view, the most that is happening now is the worldwide institutionalization of the correct appreciation: that free markets create more wealth than do markets overseen by patronage-ridden government decisions.

According to Article 1605, if an industry is nationalized in order to achieve some goal of public policy, due process must be followed and fair and adequate compensation paid. As a rule of fair play, few could object to this. According to Article 1606, there will be no restrictions on the patriation of profits or proceeds from the sale of a business, except where necessary to implement national policies relating to such events as bankruptcy and subject to balance of payments exceptions. This is a rule of a liberal capital regime and it is in Canada's self- interest to promote this into the 1990s.

Important to Canada, the Agreement exempts all Crown corporations from the national treatment obligations. Once established, national treatment provides both governments the freedom to regulate business operations in any way they wish, provided all rules and regulations apply equally to firms of both nationalities.

By maintaining their current sets of investment rules, neither country has surrendered any sovereignty. Except for changes in the conditions for review of takeovers, all investment rules are prospective. This means, for example, that Ottawa can tax foreign and domestic firms differently, provided the tax is not meant to discriminate arbitrarily between investors, and that treatment is no less favourable than that accorded one of its nationals (Article 1609).

Canada has also retained its power to discriminate between foreign and Canadian investment in certain key sectors, such as energy. According to Article 1602, for example, Canada can ensure that if Petro Canada were sold, all the shares could be bought by Canadians only. Adopting fair rules for the movement of international capital is, in any case, in the self-interest of Canada, a major foreign investor. Canada is currently the third largest foreign investor in the United States, and invests each year about three times more in the United States than Americans do in Canada. Establishing the rules of national treatment now – before the issue of foreign investment becomes a serious matter in the United States – protects Canadian investment against the kind of onslaught that Canada made against Americans through the national energy policy in the late 1970s.

With regard to investment, one of the recurring myths surrounding the free trade debate is that Canada has given up the right to nationalize and set up monopolies for nationalized industries. Article 2010 makes it clear that Canada can nationalize, provided only that it consults beforehand and pays fair compensation for firms taken over. Another myth is that Canada will be forced to harmonize standards of all sorts, which, combined with the (often fallacious) belief that our standards are better than American standards, leaves people to argue that we will be dragged down to the American level. Article 604, however, makes it clear that the two countries are to harmonize their standards only insofar as they deem mutually desirable. If Canadians do not wish to do so, they do not have to.

Another myth is that the Agreement makes it more difficult to use regional development subsidies. Prince Edward Island Premier

Ghiz recently stated this publicly in the *Financial Post*. The Agreement leaves subsidy policy exactly where it now is: subsidies (including those for regional development) are currently subject to the risk of countervail and they will be equally subject if the Agreement is signed because of the failure to agree on a subsidies code. So there is no change, neither gain nor loss of the right to subsidize. It seems odd that so many people advocate rejecting the Agreement because of what it does not say about subsidies. It seems to me that the Agreement should be judged on its pluses and minuses, not where it scores zero (as it does on subsidies).

Energy

Basically, the energy section of the Agreement legislates the *status quo*, and hence provides many pluses, especially by helping to avoid the loss of markets in such products as oil and electricity. The United States has traditionally adopted a protectionist stance against many energy imports. Protectionist measures are currently being resurrected, but they cannot be extended to Canada according to the Agreement. The Agreement will thus guarantee secure access to the U.S. market for Canadian oil and enriched uranium – where the United States is currently considering restricting imports – and for electricity, where several incipient countervail proceedings against Canadian electricity have been dropped since the Agreement was signed. Furthermore, many Canadian energy projects, such as the exploitation of the tar sands, are mega-projects that (1) cannot be profitable unless the energy is exported, and (2) cannot be financed unless the capital is imported.

In return for secure access to U.S. markets, Canada has agreed to two important restrictions. First, in the event of an emergency, Canada cannot simply turn off the tap by cancelling existing contracts. If through government fiat Canada cuts back on consumption, it must share the available supplies with the United States. Although this restates a long-standing GATT commitment, it has created great furor. It is not, however, a major restriction. To fully appreciate why proportional sharing in the event of an emergency does not create serious limitations on Canadian energy supplies, one must understand that:

- *Canada* decides unilaterally whether or not there is an emergency.
- Such energy emergencies are rare events indeed.
- Canada retains the right to control output, which is the key policy variable for conservation, since Canada is a small actor in the world energy market and can buy and sell all it wants at

the world price (which is set by forces beyond Canada's control).

- Canada already has such sharing agreements under the International Energy Agreement (IEA) and the FTA does nothing more than restate an already accepted obligation.

The second major restriction in the energy section is that a future government could not impose, as a matter of policy, a two-price system for energy products that discriminated between the domestic and the American markets. This is much misunderstood, and it is often taken to mean – for example, in both the Liberal and the NDP documents criticizing the Trade Agreement – that Canada is agreeing to a single price over all markets. This is not the case. Ontario Hydro, for example, can continue to sell its energy at different prices in different markets, getting whatever the traffic will bear. The only thing ruled out is that the Ontario government cannot pass an order in council dictating that Ontario Hydro sells at one price in the American market and at another in the Canadian.

What is ruled out, therefore, is a policy similar to the National Energy Policy of the late 1970s, where the price of Canadian oil in the domestic market was held below the world price through government decree. This is a definite restraint on future policies of this type. Most economists, however, would argue that this is not a significant concession since the policy of holding the price of any energy product below the world price is discredited by the dramatic experience of the 1970s. The world's oil crisis disappeared in the early 1980s, only after countries raised their domestic prices to the world price. On the production side, this encouraged exploration; and on the consumption side, it diminished waste by encouraging countless energy saving developments, such as the better insulation of houses. In other words, the behaviour predicted by price theory occurred when domestic oil prices were allowed to rise to the world market price, but did not occur when they were held below that price.

In any event, there are alternative instruments to achieve any objective that might be served by a two-tier energy pricing policy. If Canada wishes to subsidize Canadian industry by keeping the price of oil down, it can subsidize the industry through other methods insofar as they use our energy.

It is commonly argued, more generally, that Canada has given up the right to have an independent energy policy. This, of course, is not so. Name a legitimate object of policy, other than fleecing foreigners *per se*, and economists can find a policy tool not ruled out by the Agreement that will give effect to that policy. For example, Canadian governments can tax oil at the wellhead, they can tax consumers of oil, and they can control the rate of extraction. These policies are the key ones: taxes allow the state to appropriate resource rents (if any are accruing), and governments can control the rate of extraction to adjust for differences in the time preferences between society and private decision makers. Indeed, the government can have any policy for domestic energy resources that it wishes, as long as these policies are in pursuit of domestic goals and are not used as disguised discrimination between foreign and domestic firms and consumers.

Another myth is that Canada has given up the right to control foreign ownership in the petroleum industry. This, of course, is wrong. All policies relating to foreign ownership in the energy sector are grandfathered, including Canada's right to prevent the sale of a healthy Canadian firm to foreigners. Furthermore, pursuant to Article 1602.7, Canada can require that the shares of any privatized energy firm be sold to and held by Canadians only. Moreover, some have argued that Canada will be forced to follow whatever nonmarket policy the United States chooses to impose. If, for example, the United States takes measures to force its domestic energy prices either above or below the world prices, Article 1602.4 allows Canada the freedom to prevent itself from being dragged along by the U.S. policies.

I have time to mention only one more of the many prevalent myths: that national treatment requires the harmonization of energy and other policies between the two countries. This is not the case. National treatment allows *any* social or economic policy, including energy policy, as long as these do not become concealed barriers to trade by virtue of discriminating on the basis of nationality (except when governments are explicitly allowed to do so).

What the United States Gave Up

Finally, let us look at what the United States has given up in terms of sovereignty. Here are just a few examples.

The binational review of each country's final determinations on countervail and antidumping cases is an historic concession on the part of the United States. The United States has long been reluctant to have its national decisions subject to international review. Although review takes place in the GATT, it lacks an effective means of enforcement. The FTA allows the Canada-U.S. Trade Commission to pass judgment on the application of U.S. laws. Many trade lawyers feel that this will have a salutary effect on the way in which these laws are administered and on the decisions that are made.

Article 407, together with Articles 1101 and 1102, rules out the threat of quantitative restrictions that have been used to force foreign governments into signing Voluntary Export Restraint Agreements (VERs) with the United States. This will probably turn out to be a significant constraint on a policy tool that the Americans have used often over the last few years. Article 907 prevents the United States from cutting off Canadian access to the U.S. energy markets on national security grounds, short of a genuine shooting war. Since in the past the United States has done this to other countries on the flimsiest of national security grounds, this article is a major constraint on American sovereignty.

Article 1101 and 1102, which limit bilateral and global emergency actions taken against Canada, is a major constraint on U.S. policies that have operated frequently in the past, for example, against Canadian shakes and shingles. The circumstances under which emergency action can be taken against Canadian imports are greatly constrained, and the amount these imports can be affected is much diminished.

Lastly, by agreeing to national treatment in investment, the United States has effectively tied its hands against any anti-foreign investment policy directed at Canada – a policy that may become attractive in the 1990s when the Americans become increasingly concerned about their growing foreign ownership problem, as Canada was in the 1970s.

Conclusion

Over the months to come, you will hear and read comments that Canada has given up the right to control its energy and investment policies, and that Canada has abandoned sovereignty in many dimensions. I urge you to read the Free Trade Agreement. Then, you must interpret it in light of the GATT (on which so much of it is based), and through GATT precedents (which are part of its common law heritage). When you do so, I believe you will find that – outside of trade in goods and services, where the FTA's aim is to constrain both countries' ability to practice beggar-thy-neighbour policies – the Agreement puts minimal constraints on Canadian sovereignty. It is hard to think of a valid national policy goal that cannot be achieved through means unaffected by the Agreement. In short, although some *policy instruments* are constrained, alternatives exist in virtually all cases so that our ability to attain *policy goals* is not.

Notes

1. See C.D. Howe Institute, *Policy Harmonization: The Effects of a Canadian-American Free Trade Area* (Toronto: C.D. Howe Institute, 1986), especially the Introduction and Chapter 1.

2. See "Sovereignty" in J. Crispo ed., *Free Trade: The Real Story* (Toronto: Gage Publishers, 1988).

Will the Free Trade Agreement Affect Canada's Sovereignty?

Lloyd Axworthy

The opportunity to speak with you about sovereignty is a great pleasure. I have looked at the lineup of speakers and presenters, and at the papers that are being given, and I have noticed that the distinct and unmistakable train of thought throughout this exercise is the assumption that the Free Trade Agreement (FTA) is a *fait accompli*, and that now it is just a question of time to see exactly what kind of business we can do with it. In a sense, I feel as though I am appearing before the college of cardinals speaking about abortion, since I am sure that you have been following the press and that you know that I don't like this Agreement. I believe the FTA is a threat to this country and I wish to present a case that I hope some of you will consider before we're through.

It is quite entertaining to share this platform with Mr. Lipsey, one of the charter members of the evangelical movement of messianic economists who have promoted this particular thesis for years. I need not remind you of the plague over the GATT, where the evangelical right was so busy talking about what was right that it forgot what was good. Perhaps this is part of the problem we face today with the FTA.

I would also like to comment on this conference. I am impressed and amazed that all of you are still here on a Friday afternoon after 5:30. I just came from duty day at the House of Commons; I thought *we* were crazy. I suppose this proves that Mr. Mulroney was correct when he predicted jobs; he created a cottage industry with free trade in the form of trade conferences.

I represent a different constituency than most of you in this room. I represent not only the good people of Winnipeg whom Maxwell Cohen talks about, but all Canadians, measured by the opinion polls and the people I see on the streets. I have heard the thoughts of nurses, teachers, workers, students, artists and cultural people, and a large number of Canadians are uneasy about free trade. The people are confused by it; there is a real sense of apprehension about it, and something tells me it's not over yet. If any of you believe the FTA to be a *fait accompli* awaiting only the finer details, then you had better take another look. We have the commitment of two political parties presently representing 68 per cent of the voting public, which clearly indicates that the FTA should be scrapped, not for rhetorical reasons, but to reflect and respond to our constituencies.

The FTA has a lot more to it than that suggested in the minimalist position taken by Mr. Lipsey. Free trade is not a trifle, nor is it merely a small bag of tricks or simply a question of reducing a few tariffs and changing a few rules on industrial procedures; it goes beyond that. And, it surprises me to hear Mr. Lipsey downplay the significance of the FTA when in his writings he has referred to it as the most historic, valuable and important mental happening in the history of Canada – the great Armageddon. I partially agree with Mr. Lipsey in his writings, although I reserve Confederation itself as Canada's most important event. Now *that* was an act of political will that ran against all the currents of the market system, of geography, of economics and probably even good sense, as political acts often do.

Each successive generation has used various tools and instruments of government to forge the curious conglomeration we call Canada. Our history represents a very clear set of choices made by Canadians over the years to initiate institutions, practices, policies and programs, a multitude of policy initiatives which combined have created our country.

At issue in the free trade debate is whether this political autonomy can be maintained, whether the government and the public sector can continue to make at least an equal range of choices, and engage in their legitimate public debate. It is at this point where I would like to underline a very interesting point mentioned by Professor Harrison. With regard to energy policy, he noted that the Agreement simply reflects the present level of policy in energy between United States and Canada: decentralization, privatization and deregulation. But, he said, the FTA also represents a major constraint on future policies. This is the issue, not the fact that Liberals and Conservatives will be debating the Agreement in the future. Once the Agreement is signed it is "entrenched," as

Mr. Lipsey politely said. It then becomes untouchable by future generations. In other words, it becomes much tougher to make changes if and when the political constituency of Canada requires, wants or demands.

This problem is part of a general trend, including the Meech Lake Accord and the rest of the changes that have been going on: we envisage the capacity of government to make these types of choices, but we are removing the choices from the public realm of political debate and discussion. We are moving away from the kind of political process that is absolutely essential to keep this country going. This is the essense of Canadian sovereignty and I believe that this is where the debate has become somewhat skewered.

I am a member of the political party which has sought and achieved substantial liberalization of trade over several decades, and I know that through international rules and various negotiations, Canada has been able to minimize the kind of concessions that are required of liberalization. We still believe that our formula is effective. We should not be overly concerned about the philosophy of free trade, because the specific deal, the FTA, goes way beyond issues of trade; it reaches far beyond the categories that Mr. Lipsey spoke of. It is not just energy and investment, but agriculture, subsidies and institutions.

I had been involved in the question of the movement of western coal to Ontario to supply American industry. We are all aware of the mathematics of that issue: Ontario reduced its emissions by 50 per cent by the year 1990-1991. Canada had a choice: spend a couple of billion dollars on scrubbers, or buy clean coal from Western Canada. We were looking for ways in which Canada could bring the movement of coal within economic possibilities, and we arranged for a draft policy for transportation subsidization of about $10 per tonne. This was all right because the economic benefits, we could argue, were pretty substantial. In Western Canada there were about $6 or $7 billion of capital investments, many jobs and a transportation line right into Ontario. The point is, transportation subsidies, one of the traditional and effective public policy choices used by Canada as a means of regional development, will not be possible under the Agreement. We could not tell our new economic partners that we are no longer going to buy a billion dollars worth of Ohio coal every year because we are going to subsidize western coal to come into Ontario without risking retaliation under U.S. trade law.

So that is one option lost, and it should be up to Canadians to make this type of choice, not Americans. Moreover, I would suggest to you that the U.S. definition of subsidy, which may be reinforced under future trade law if the omnibus bill goes through, is substantially different from that under international trade law.

The elimination of freedom of choice is only one major concession. We must also look to areas outside of the Agreement. Mr. Lipsey and Mr. Smith have written a book about harmonization. This subject has been critically examined in front of the Special Commons Committee. There has been testimony from people who philosophically believe in free trade that key to the Agreement is the implementation of the principle of national treatment. Almost every organization will put pressure on the kind of wage laws, environment standards and occupational laws that Canada now has. To duck this issue is to say that somehow competition is a theoretical, abstract notion which is, simply, unrealistic.

Do we want to take away the kind of public policy instruments and institutions that Canada now has in order to follow the marketplace theology inherent in this particular agreement? This is really what the debate is about. It is not so much about trade because the so-called economic benefits are marginal. This is supported by the week-old Department of Finance report: one half of 1 per cent of GNP growth per year; 20 000 to 25 000 jobs per year. And this does not include the $2 billion in lost revenue for customs.

Why are we pushing free trade if the economics of it are marginal? I believe that there is a serious intent on the part of many Canadians to ensure that future governments do not do things like NEBs or performance requirements under the FIRA. But the mistake that these people are making – and this is where the sovereignty issue comes in – is they want to entrench this. Canadian trade autonomy will thus be moved outside of the Canadian political process since our international trading partners will not be prepared to deal with the cycles of Canadian politics.

The multinationals and the U.S. administration did not like the NEB for various reasons, but we believe that we were elected to implement it. We believe that the NEB was a legitimate choice. Future governments may want the same choices, the same freedom to make choices, and to be able to use the instruments of public policy to achieve industrial, economic or social objectives. If a trade agreement like the FTA becomes entrenched, issues such as these are no longer political; they are placed outside that framework.

This is the agenda we are talking about. We are talking less about trade and more about whether Canada is applying general market policy as opposed to political autonomy in the management of this country. This is the substantive issue that is dividing Canadians in a very dramatic and controversial way.

Strengthening Canada's Position in the GATT

Jean J. Charest

This afternoon I would like to contribute something slightly different from the largely technical analysis we have been hearing. Instead, I would like to review the broader perspective – the global issues that arise from the Agreement.

As it is frequently pointed out, the international economy is becoming more and more interdependent. Of course, this is demonstrated most clearly by the collective volatility of world stock markets in recent months. "Interdependence" is also the catchword to describe the economies of Canada and the United States. Today, the pressing question is: how do we ensure the greatest national benefit from this interdependence? In essence, this is question of management.

Naturally, the first logical step is a more effective management of the Canada-United States trading relationship. For Canada, this means attaining a more secure and predictable access to the U.S. market, and this is precisely what Canada has accomplished in the Canada-U.S. Free Trade Agreement. The Prime Minister has referred to the Canada-U.S. trade initiative as "a declaration of confidence in ourselves. Confidence in our ability to compete with the best in the world. Confidence in our ability to adapt in a tough and demanding world environment." The same is true of Canada's efforts to liberalize trade with its GATT partners in the Uruguay Round underway in Geneva.

As many of you know, the Canadian Government's trade policy operates on two tracks to liberalize trade: with its principal trading partner, the United States, as well as with its other GATT partners in the ongoing Uruguay Round. With the completion of the Canada-U.S. Agreement, Canada has completed half the job. The remaining half – in the Uruguay Round – is in progress.

Minister Carney has made it clear – most recently at the Asian-Pacific Trade Conference in Bali a few weeks ago – that Canada would be pleased to host a midterm review of the Uruguay Round toward the end of 1988. We believe that it will be essential to take stock of developments in the negotiations, to tie down progress and to set the stage for the concluding phase of the Round.

Canada has always believed that the GATT is the best available institution for ensuring that global trade is as free and as fair as possible. Even as Canada has engaged in negotiations with the United States, it has maintained a strong commitment to the GATT and the current Uruguay Round.

In December, Minister Carney attended the 40th anniversary of the Contracting Parties of the GATT. There she reaffirmed that commitment and spelled out the key Canadian objectives in the Uruguay Round. I think these bear repeating this afternoon:

- First, strengthening the GATT system. We need to transform the GATT from an organization that administers an international trade agreement into a more active policy-oriented institution.

- Second, developing new rules and better access for agricultural trade. The Uruguay Round must achieve basic reform of trade-distorting agricultural policies. Canada is, of course, working with the Cairns Group of Fair Agricultural Traders to make progress in this area.

- Third, improving and securing market access. These issues have been the key element of GATT negotiations over the past 40 years and represent a major objective in this Round.

- Fourth, focusing on the so-called new issues, namely, trade in services, and the trade-related aspects of intellectual property and investment measures.

- Finally, ensuring greater participation and integration of developing countries into the GATT. Canada is committed to working with developing countries in the current Round to ensure that the results include those issues of importance to them. At the same time, it is essential that each country, particularly the newly industrialized nations, become fully integrated into the multilateral trading system and take on appropriate obligations for its effective operation.

In the Uruguay Round, we believe that the ground breaking progess Canada and the U.S. have made bilaterally on certain key issues, such as trade in services, will stand us in good stead. The reasons are simple. For one thing, we have thought our way through some of these complex new issues. Moreover, what the Canada-U.S. Agreement clearly demonstrates is that countries can find solutions to even the most thorny trade problems when there is a firm political will to do so. In this way, the Canada-U.S. Agreement has implications that go far beyond bilateral trade; it sends a positive message to other partners in the international trading community, a message about fighting protectionism.

History has shown that Canada has prospered as it has reduced barriers to its trade. Today, however, new and insidious forms of protectionism in foreign markets are threatening the interests of our farmers, manufacturers and service industries. The Canada-U.S. Agreement provides a powerful signal against protectionism and for trade liberalization. It reflects the same commitment of the Canadian government to liberalize trade which animates our active participation in the multilateral trade negotiations under the GATT.

I would like to close with the words of a former president of the Canadian Manufacturers' Association who said: "We are not manufacturers merely of articles; . . . we manufacture enthusiasms; . . . we manufacture a feeling of pride in our country, and we manufacture a spirit of independence." This is the spirit behind the Canada-U.S. Free Trade Agreement. It is the spirit of those who believe that Canadian industry and workers rank with the best the world has to offer.

This is also the spirit behind Canada's participation in the Uruguay Round. It is our hope that the work Canada and the United States have accomplished together will spur the negotiations in Geneva toward an equally historic agreement in trade liberalization worldwide.

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Edited by Donald M. McRae and Debra P. Steger

The Canada-U.S. Free Trade Agreement signed on January 2, 1988 remains the subject of intense public debate among Canadians. This volume presents the proceedings of a conference co-sponsored by the University of Ottawa Faculty of Law (Community Law Section), the Canadian Council on International Law and the Institute for Research on Public Policy held in Ottawa on January 22, 1988. The authors, all leading Canadian and U.S. international trade experts, present extensive analysis of this historic Agreement and examine the specific policy implications in the context of Canada's existing international obligations. Topics discussed include the subtleties of the dispute resolution procedures, specific issues involved in the adoption of the principle of national treatment, and the constitutional dimensions of domestic implementation of the Agreement. The implications for Canada's sovereignty are also considered. This distinguished group of lawyers and trade policy specialists provide an authoritative analysis of the implications of implementation of the Free Trade Agreement for future public policy directions in Canada.

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